# ENTREPRENEURSHIP AND MANAGEMENT CONCEPTS

Dr. Vikas Saraf
Pawan Thakur
Lata Yadav

# ENTREPRENEURSHIP AND MANAGEMENT CONCEPTS

In Accordance with Syllabus Prescribed by
Rajiv Gandhi Technical University, Bhopal

***For V Semester B.Tech Students of***

- Mechanical Engineering
- Automobile Engineering
- Production Engineering
- Industrial Engineering
  and other Related Branches

**RGTU**



**Dr. Vikas Saraf**
**Pawan Thakur**
**Lata Yadav**

# Entrepreneurship and Management Concepts

## AU/IP/ME/TX/CM-501 (RGTU)

**Unit-I: System Concepts:** Types, definition & characteristics; supra & subsystems, key component; boundary & interface complexity; feedback (pull) & feed forward (push) controls, open flexible-adaptive system, computer as closed system, law of requisite variety; system coupling, stresses and entropy; functional & cross functional system; Steven Alter's nine element work system model and its comparison with IPO (input-processing-output) model, structure and performance of work systems leading to customer delight.

**Unit-II: Management:** Importance, definition and functions; schools of theories, knowledge driven learning organization and e-business; environment, uncertainty and adaptability; corporate culture, difficulties and levels of planning, BCG matrix, SWOT analysis, steps in decision-making, structured and unstructured decision; dimensions of organizations, size/specialization, behaviour formalization, authority centralization, departmentalization, spam and line of control, technology and Minzberg organization typology, line, staff & matrix organization, coordination by task force, business process reengineering and process of change management, HR planning placement and training, MIS; attitudes and personality trait, overlap and differences between leader & manager, leadership grid, motivation, Maslow's need hierarchy and Herzberg two factor theory, expectation theory, learning process, team work and stress management.

**Unit-III: Marketing:** Importance, definition, core concepts of need want and demand, exchange & relationships, product value, cost and satisfaction (goods and services ) marketing environment; selling, marketing and societal marketing concepts; four P's, product, price, placement, promotion; consumer, business and industrial market, market targeting, advertising, publicity, CRM and market research.

**Finance:** Nature and scope, forms of business ownerships, balance sheet, profit and loss account, fund flow and cash flow statements, breakeven point (BEP) and financial ratio analysis, pay-back period, NPV and capital budgeting.

**Unit-IV: Productivity and Operations:** Productivity, standard of living and happiness, types of productivity, operations (goods and services) Vs project management, production processes and layouts, steps in method improvement, time measurement, rating and various allowances; standard time and its utility, predetermined motion and time method, product and process specification, TQM, cost of quality, introduction to lean manufacturing (JIT), QFD, TPM & six sigma quality.

**Unit V: Entrepreneurship** : Definition and concepts, characteristics, comparison with manager, classification, theories of entrepreneur, socio, economic, cultural and psychological; entrepreneur traits and behaviour, roles in economic growth, employment, social stability, export promotion and indigenization, creating a venture, opportunity analysis competitive and technical factors, sources of funds, entrepreneur development programme.

# ENTREPRENEURSHIP AND MANAGEMENT CONCEPTS

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# Preface

This book is intended basic concepts of Entrepreneurship and Management Concepts. Entrepreneurship is a fundamental source of change in all aspects of society, empowering individuals to seek opportunities where others see undefeatable problems. For the past century, entrepreneurs have created many great enterprises that subsequently led to job creation, improved productivity, increased prosperity, and a higher quality of life. Entrepreneurship is now playing a vital role in finding solutions to the huge challenges facing civilisation, including energy, environment, health, security, and education.

Each chapter of this book contains student learning activities to give the readers a chance to enhance the learning process. We show the critical differences between scientific ideas and true business opportunities. Readers benefit from the book's integrated set of examples, business plans and recommended sources for more information.

This book on Entrepreneurship and Management Concepts has been written for the undergraduate students of B.E., B. Tech., B.B.A, B. Com., B.A., and postgraduate students of M.B.A., M.S.W., M.Com, M.C.M, P.G.D.M, and similar courses of various Universities of Madhya Pradesh, Chhattisgarh, Uttar Pradesh, Rajasthan, Haryana and other Indian Universities. This book is divided in to Six Unit.

**Unit I**, presents the basic concepts of system, controlling coupling and models of system like types of system, components of system, super and subsystem, feedback (pull) & feed forward (push) controls, open flexible-adaptive system, computer as closed system, law of requisite variety and work systems leading to customer delight.

**Unit II**, we bring, management roles and functions in business plan, functions of management, knowledge driven learning organization and e-business, environment, uncertainty and adaptability, partnership and cooperative committees, elements effects selecting the form of organization, concentrates on the areas of organisation plan, nature and purpose of organization, principles of organization, and dimensions of organizations, departmentalization, and matrix organisation, concept of planning, re-engineering and process of change management, BCG matrix, McKinsey GE Matrix, SWOT analysis, attitudes and personality trait, differences between leader & manager and leadership grid.

**Unit III**, deals with the concepts of marketing plan, 4P's of marketing mix, business and industrial market, market segmentation, targeting and positioning, advertising, publicity, CRM market research and finance management like balance sheet Profit and Loss account (P & L A/C), Working Capital, Management, Fund flow and Cash flow statements, Break Even Point (BEP) and Financial ratio analysis.

**Unit IV**, we evaluate and examine productivity and operations like standard of living and happiness, types of productivity, production processes and layouts economic order quantity (EOQ), ABC-Analysis, XYZ-analysis and method improvement and models such as steps in method improvement, time Measurement, lean manufacturing – Just-in-Time (JIT), six sigma quality (6σ), SCM, and enterprise resource planning (ERP).

**Unit V**, we present the theoretical concepts of entrepreneurship and innovation like characteristics of entrepreneur, key qualities of entrepreneur, and types of entrepreneur nature and characteristics of entrepreneurship, importance of entrepreneurship and we evaluate and examine innovation as a strategy, various theories of entrepreneur, entrepreneur traits and various sources of funds.

**Unit VI**, focuses on the concept of project identification and formulation, scanning of business environment and identifying and projects and project identification for an existing company and preparation of business plan or project report, guidelines by planning commission for project report, identification of business opportunities, project report evaluations.

**—Dr. Vikas Saraf**

**— Pawan Thakur**

**— Lata Yadav**

# Acknowledgement

Our efforts are never truly individual they are the result of the collective inputs of several people who have inspired, supported and empowered us in many ways. We have assisted by our teachers, colleagues and students—too many name, but are very special who have helped us sharpen our thinking by cheerfully providing challenging comments and questions.

I, Dr. Vikas Saraf would like to thanks all the people who contributed to this book. The timely completion of this book is mainly due to the concern of my father Shri Subhash Saraf & my mother Smt. Maya Saraf. Their contribution will be remembered forever.

My sincere thanks to Shri Suresh Jain IAS, Managing Director, Vidyasagar Institute of Management for his continuous support and encouragement for writing this book.

I would like to give special thanks to my wife Smt. Sarika Saraf for her patience, continuous encouragement during the preparation of this book and thank to my daughter Ku. Vedika and son Master Videh, who tolerated Papa's refusals to take them on outings.

**— Dr. Vikas Saraf**

I, Pawan Thakur first of all would like to extend remarkable thanks to my parents and family members. My special thanks to late. Shri Hari Chand Thakur who was not only my father and teacher but also a good friend and guide, their contribution will be remembered forever. I am thankful to my mother Mrs. Kunta Devi, without their blessing and valuable support this could not be achievable.

My special thanks are due to my lovely wife Ms. Sikkma Devi, my amazing brother Mr. Ram Krishan his wife Ms. Jyoti Thakur for bearing with me when I used to spend long hours on my PC while writing this book. My extraordinary thanks are due to my little and cute son Master Sarthak Thakur—without you this would not have been possible.

The idea of this book was planned by Dr. Vikas Saraf, Director, Vidyasagar Institute of Management. My Special thanks are due to him not for the idea but also the encouragement and unstinted support throughout in this project.

**— Pawan Thakur**

I, Lata Yadav would indebted to my parents Shri P.L. Yadav & Smt. Urmilla Yadav, who have always taught me to excel. I am grateful to my family specially my in-laws and my younger sister Ms. Manisha Yadav, who have truly participated in my labour. Their belief in me has helped me to channelize my energy, this could not be possible without the emotional and psychological encouragement of my wonderful husband Sanjay and my beloved son Atharva for their priceless support and help at every step thank you for this.

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Finally, I am also profoundly grateful to all the faculty, staff member and student of VIM Bhopal, and other Professors, learning facilitators, and students who shall use this book.

**— Lata Yadav**

From all the three authors, A special word of thanks is to the team of **M/s Kataria & Sons** for accepting our proposal in bringing out this book in nice and striking form.

# Contents

# 1 Basic Concepts of System

**Chapter Outline**



## 1.1 INTRODUCTION

A system is a set of components that interact to accomplish some purpose. e.g., college system, economic system, language system, a business and its parts - marketing, sales, research, shipping, accounting, government. In business, system analysis and design refers to the process of examining a business situation with the objective of improving it through better procedures and methods. System analysis and design relates to shaping organizations, improving performance and achieving objectives for profitability and growth. The emphasis is on systems in action, the relationships among sub-systems and their contribution to meeting a common goal.

A system is designed to achieve one or more objectives. We are in daily contact with the some system likes transportation system, the telephone system, the accounting system, the production system, and, for over two decades, the computer system. Similarly, the business system of the organization is a system of consisting of interrelated departments (sub-systems) such as production, sales, personnel, and an information system. The sub-systems are of much use as a single, independent unit. When they are properly coordinated, however, the firm can function effectively and profitably. The process is examining of a (business) situation with the intent of improving it through better procedures and methods.

(i) **System Analysis:** The process of gathering and interpreting facts, diagnosing problems, and using the facts to improve the system is known as system analysis.

(ii) **Systems Design:** The process of planning a new system to replace or complement the old is known as system design. Analysis specifies what the system should do and design states how to achieve the objective.

## 1.2 MEANING AND DEFINITION

The term system is derived form the Greek word systema, which means an organized relationship among functioning units or components. There are more than a hundred definitions of the word system, but most seem to have a common approach:

**Important Point:** *"A system is an orderly grouping of interdependent components linked together according to a plan to achieve a specific objective."*

- *"A system is a set of components that interact with one another and serve for a common purpose or goal."*
- *"A system is a collection of objects such as people, resources, concepts, and procedures intended to perform an identifiable function or to serve a goal."*

Basically there are three major components in every system, namely input, processing and output as shown in Fig. 1.1.

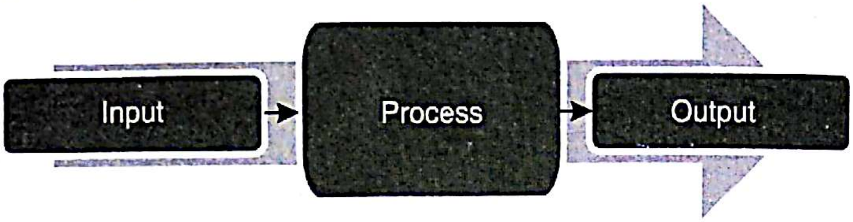


Fig. 1.1 Major components of System

In a system the different components are connected with each other and they are interdependent. For example, human body represents a complete natural system. We are also bound by many national systems such as political system, economic system, educational system and so forth.

The objective of the system demands that some output is produced as a result of processing the suitable inputs. The following Fig. 1.2 showed an example of fast food restaurant as a system:

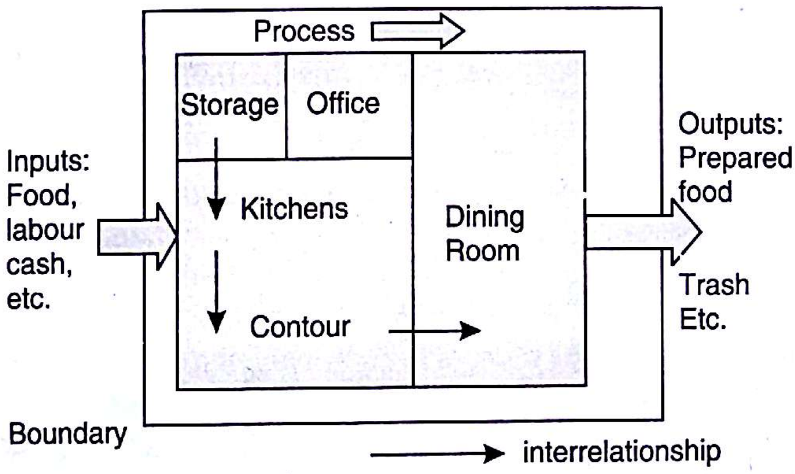


Fig. 1.2 Fast food restaurant as a system

## 1.3 CHARACTERISTICS OF SYSTEM

The above definitions of a system represent the characteristics of systems as: organization (order), interaction, interdependence, integration and a central objective as shown in Fig. 1.3.

1. **Central objective:** A system is designed to achieve one central objective. Objectives may be real or stated. Although a stated objective may be the real objective, it is not uncommon for an organization to state one objective and operates to achieve another.

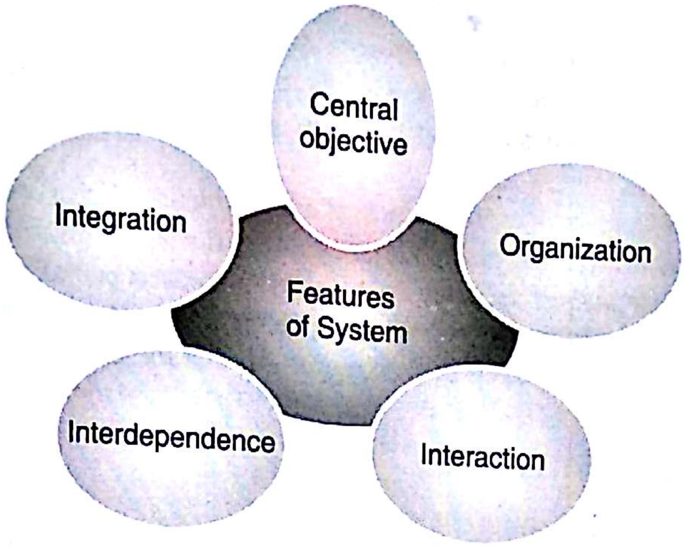


**Fig. 1.3** Features of System

The important point is that users must know the central objective of a computer application early in the analysis for a successful design and conversion. Political as well as organizational considerations often cloud the real objective. This means that the analyst must work.

2. **Organization:** Organization means structure and order that is arrangement of components that helps to achieve objectives. In the design of a business system, for example, the hierarchical relationships starting with the president on top and leading downward to the blue – collar workers represents the organization structure as shown in the Fig. 1.4.

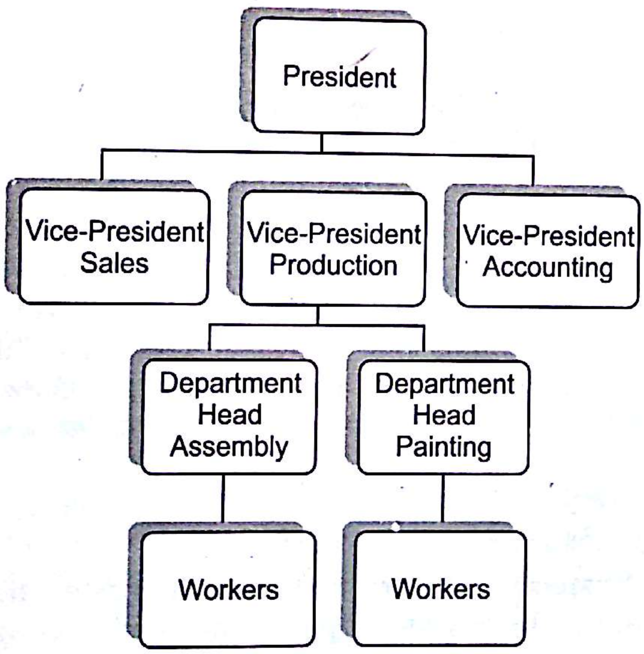


**Fig. 1.4** Structure of organization

3. **Interaction:** Interaction refers to the manner in which each component of the system functions with other components of the system. In an organization, for example, purchasing must interact with production, advertising with sales and payroll with personnel.
4. **Interdependence:** Interdependence means that parts of the organization depend on one another in a system. They are coordinated and linked together according to a plan. One sub-system depends on the input of another sub-system for proper functioning: that is, the output of one sub-system is the required input for another sub-system. This interdependence is crucial in systems work.
5. **Integration:** Integration is concerned with how a system is tied together. It is more than sharing a physical part or location. It means that parts of the system work together within the system even though each part performs a unique function. Successful integration will typically produce a synergistic effect and greater total impact than if each component works separately.

## 1.4 TYPES OF SYSTEM

Systems are classified in different ways:

1. **Physical or abstract systems:** A physical system, in contrast, has a material nature. It is based on material basis rather than on ideas or theoretical notions. For example, the physical parts of the computer center are the officers, desks, and chairs that facilitate operation of the computer. They can be seen and counted and also they are static as shown in the Fig. 1.5.

**Fig. 1.5** Physical system

In other hand, abstract systems are conceptual or non-physical entities. An abstract system is conceptual, a product of a human mind. That is, it cannot be seen or pointed to as an existing entity. Social, theological, cultural systems are abstract systems. None of them can be photographed, drawn or otherwise physically pictured. However, they do exist and can be discussed, studied and analyzed.

2. **Open or Closed Systems:** Another classification of systems is based on their degree of independence.
   (i) **Open System:** A system that interfaces and interacts with its environment, by receiving inputs from and delivering outputs to the

outside is called an open system. They possess permeable boundaries that permit interaction across its boundary, through which new information or ideas are readily absorbed, permitting the incorporation and diffusion of viable, new ideas as shown in Fig. 1.6.

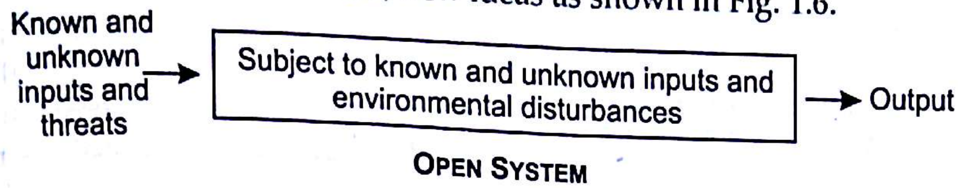


Fig. 1.6 Open System

Examples of open systems: Business organization, Hospital system, College or University system.

(ii) **Close system:** A system that does not interact with their environment is known as close system as shown in Fig. 1.7. In contrast, a closed system is isolated from environmental influences. In reality, a completely closed system is rare. In systems analysis, organizations, applications and computers are invariably open, dynamic systems influenced by their environment.

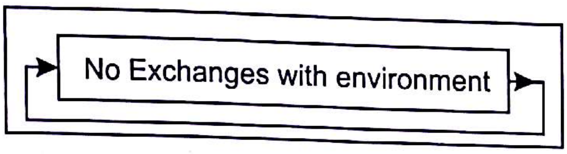


Fig. 1.7 Close System

3. **Man Made Information Systems:** An information system is the basis for interaction between the user and the analyst. It provides instruction, commands and feedback. It determines the nature of the relationships among decision-makers. In fact, it may be viewed as a decision center for personnel at all levels. From this basis, an information system may be defined as a set of devices, procedures and operating systems designed around user based criteria to produce information and communicate it to the user for planning, control and performance. In systems analysis, it is important to keep in mind that considering an alternative system means improving one or more of these criteria.

   A good example of this would be something that is known as a Management Information System or MIS for short. An MIS is a collection of people, processes and resources that are used together in order to help managers and senior members of staff to make effective decisions. To give you an example in context, you could consider a school. The MIS system of this school will operate to give the head teacher and members of the school council the information they need to make effective decisions.

4. **Formal and Informal Information system:** A formal information system is based on the organization represented by the organization chart. The chart is a map of position and their authority relationship, indicated by boxes and connected by straight lines. It is concerned with the pattern of authority, communication and work flow. The Fig. 1.8 shown the organizational chart of the top level positions at a university.

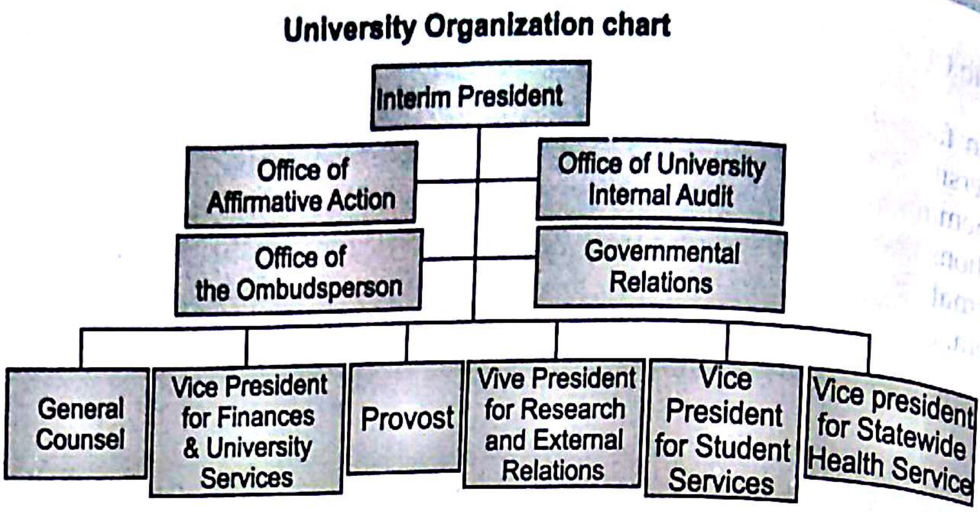


**Fig. 1.8** Formal Information System

The informal information system is employee based system design to meet personnel and vocational needs and to help in the solution of work-related problems. It also funnels information upward through indirect channels. In this way, it is considered to be a useful system because it works within the framework of the business and its stated policies.

In other words, the informal information system should be employee based and cater to their development and solve their work related problem. Employee co-operation and the knowledge of the informal communication should help one to get a good Informal Information Systems in place.

5. **Computer based information systems:** A computer based information system is an organised integration of hardware and software technologies and human elements designed to produce timely, integrated, accurate and useful information for decision making purposes.

## 1.5 SUPRA AND SUB-SYSTEMS

The larger units involving a system are called supra-system or environment, and the smaller unit enclosing a system is called a sub-systems or components as shown in Fig. 1.9.

(i) **Supra-system:** The environment is the "supra-system" within which an organization operates. It is the source of external elements that impinge on the system.

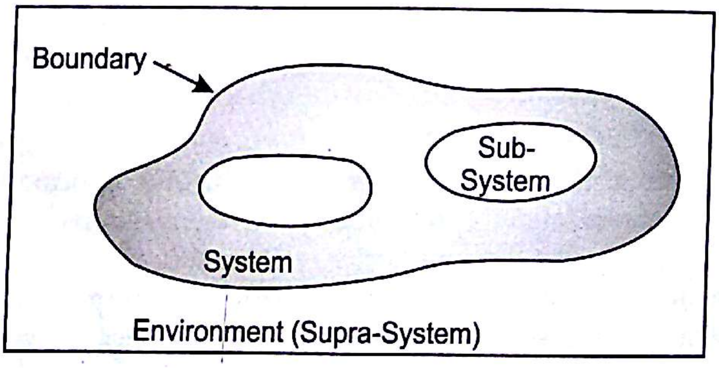


**Fig. 1.9** Supra & Sub-Systems

In fact, it often determines how a system must function. For example, a university has different branches like: management, arts, science, computers, mathematics etc., each of these branches can be observed as a smaller unit which functions independently. Examples of university system branches include a student information system (SIS), a library information system, a faculty information system, and a finance system, as illustrated in Fig. 1.10.

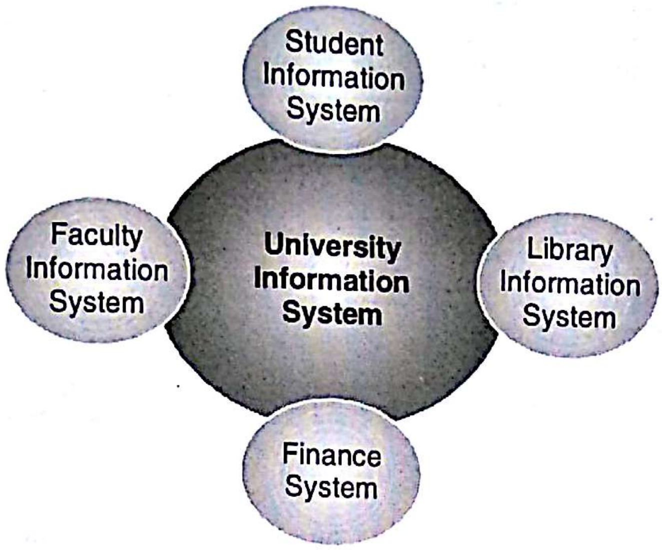


**Fig. 1.10** University Information System

For another example supra-system of a family may be the church community or ethnic group to which it belongs. A supra system is the larger unit comprises smaller units.

**(ii) Sub-systems:** A system and its environment can be described in many ways. A sub-system is a part of a larger system. Each system is composed of sub-systems, which in turn are made up of other sub-systems, system being delineated by its boundaries. For example, the sub-systems of a Business System are as follows as shown in Fig. 1.11:

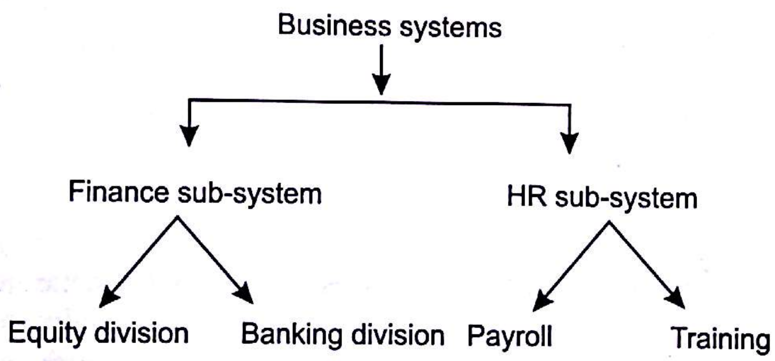


**Fig. 1.11** Business System

The different sub-systems of a computer system are shown in Fig. 1.12 Such as input sub-system, storage sub-system, processing sub-system output sub-system, etc.

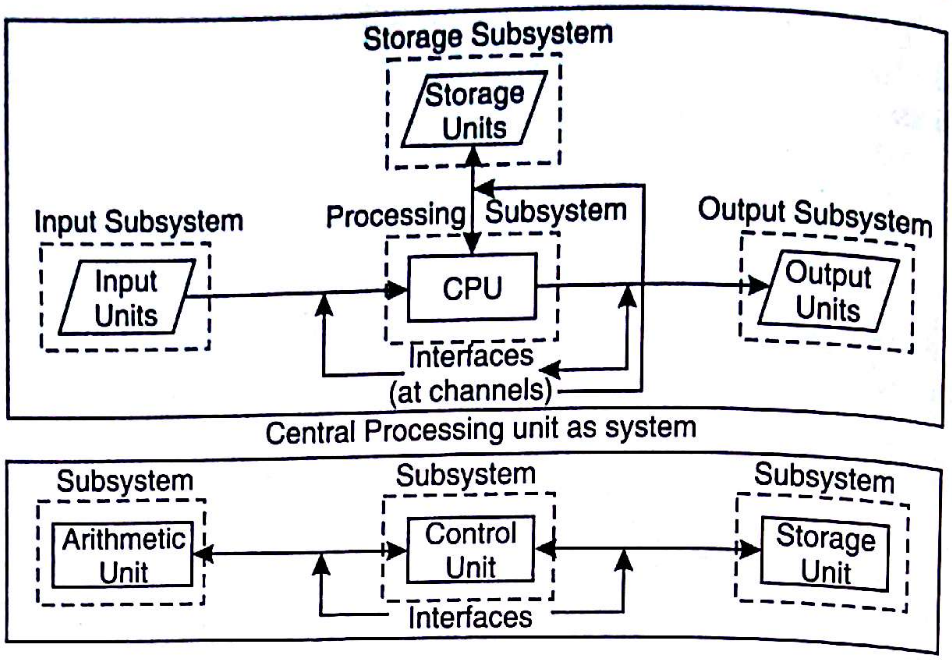


**Fig. 1.12 Sub-Systems of a Computer System**

## 1.6 KEY COMPONENT OF SYSTEM

A system has following key elements or components as shown in Fig. 1.13. A component is either an irreducible part or an aggregate of parts, also called a sub-system. The simple concept of a component is very powerful. For example, in case of an automobile we can repair or upgrade the system by changing individual components without having to make changes the entire system.

1. **Input**: A major objective of a system is to produce an output that has value to its user. Whatever the nature of the output (goods, services, or information), it must be in line with the expectations of the intended user. Input includes machines, manpower, raw materials, money, time, etc.
2. **Output**: These are information in the right format, conveyed at the right time and place to the right person.
3. **Interrelated**: The components are interrelated that is the function of one is somehow tied to the function of the others. For example, in the Store system the work of one component, such as producing a daily report of customer orders, may not progress successfully until the work of another component is finished, such as sorting customer orders by date of receipt.
4. **Interface**: The point at which the system meets its environment are called interface.
5. **Boundary**: A system has a boundary, within which all of its components are contained and which establishes the limits of a system, separating it from other systems.
6. **Environment**: A system operates within an environment everything outside the system's boundary. The environment surrounds the system, both affecting it and being affected by it. For example, the environment of a university includes prospective students, foundations, funding agencies and the new media. Usually the system interacts with its environment. A university interacts with prospective students by having open houses and recruiting from local high schools.

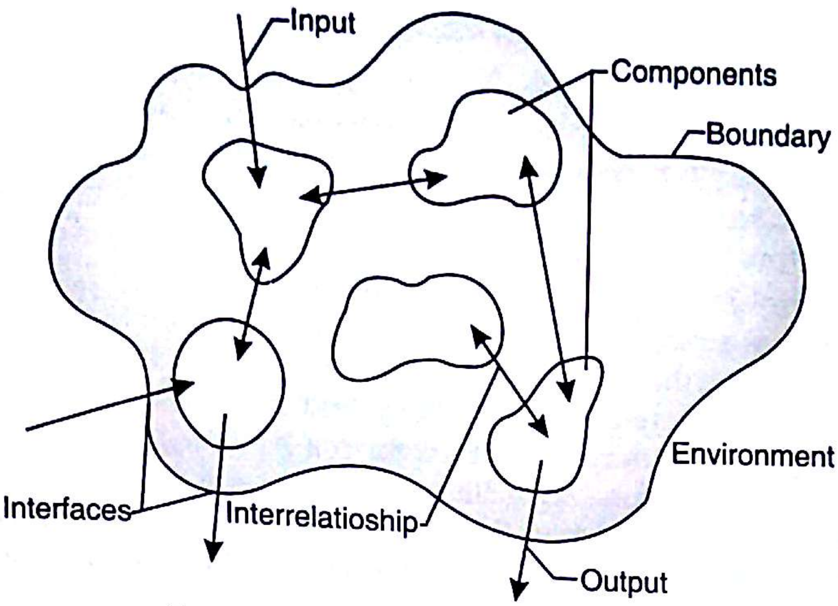


Fig. 1.13 Key Component of a System

## 1.7 BOUNDARY AND INTERFACE COMPLEXITY

A system should be defined by its boundaries the limits that identify its components, processes and interrelationship when it interfaces with another system as shown in Fig.1.14. For example, a teller system in a commercial bank is restricted to the deposits, withdrawals and related activities of customers checking and savings accounts. It may exclude mortgage foreclosures, trust activities, and the like.

1. **Boundaries:** Each system has boundaries as shown in the Fig. 1.14, that determine its sphere of influence and control. All systems function within some sort of environment, which is a collection of elements. These elements surround the system and often interact with it. For any given problem, there are many types of systems and many types of environments. Thus, it is important to be clear about what constitutes the system and the environment of interest. The features that define and delineate a system from its boundary. The system is inside the boundary the environment is outside the boundary.

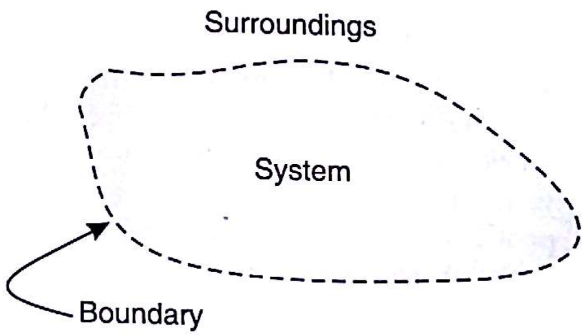


Fig. 1.14 Boundaries and Interface Complexity

In some cases, it is fairly simple to define what part of the system is and what is not. Within the boundary of a system we can find three kinds of *properties*:

(i) **Elements:** These are the kinds of parts (things or substances) that make up a system. These parts may be atoms or molecules, or larger bodies of matter like sand grains, rain drops, plants, animals, etc.

(ii) **Attributes:** These are characteristics of the elements that may be perceived and measured. For example: quantity, size, color, volume, temperature, and mass.

(iii) **Relationships:** These are the associations that occur between elements and attributes. These associations are based on cause and effect.

(iv) **Interface complexity:** Point of contact where a system meets its environment or where sub-systems meet each other.

For example, in an integrated banking wide computer system design, a customer who has a mortgage and a checking account with the same bank may write a check through the teller system to pay the premium that is later processed by the "mortgage loan system. Recently, system design has been successful in allowing the automatic transfer of funds form a bank account to pay bills and other obligations to creditors, regardless of distance or location. This means that in systems analysis, knowledge of the boundaries of a given system is crucial in determining the nature of its interface with other systems for successful design.

## 1.8 FEEDBACK (PULL) & FEED FORWARD (PUSH) CONTROLS

System feedback is a loop wherein information of some kind is fed back into the system. In this way, the system can respond to its environment. A typical example of a feedback system is shown in Fig.1.15 Input into a system, together with an unknown quantity labeled disturbances, results in an output which is fed back into the system again.

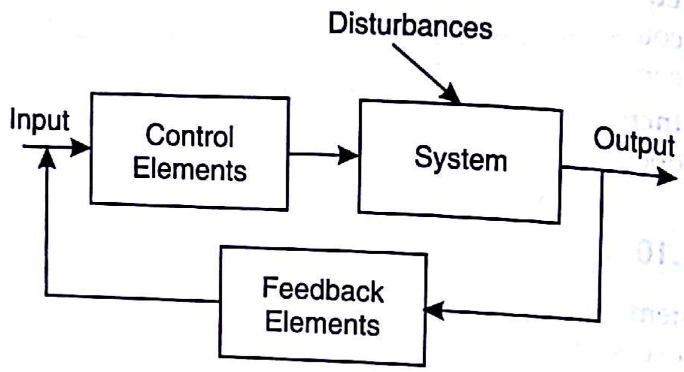


**Fig. 1.15** Feedback System

There are two main kinds of feedback control :

(i) **Feedback (Pull) controls:** It involves reviewing information to determine whether performance meets established standards. For example, suppose that an organization establishes a goal of increasing its profit by 12 percent next year. To ensure that this goal is reached, the organization must monitor its profit on a monthly basis. After three months, if profit has increased by 3 percent, management might assume that plans are going according to schedule.

(ii) **Feed Forward (Push) Controls:** Sometimes called preliminary or preventive controls, attempt to identify and prevent deviations in the standards before they occur. Feed forward controls focus on human, material, and financial resources within the organization. These controls are evident in the selection and hiring of new employees. For example, organizations attempt to improve the likelihood that employees will perform up to standards by identifying the necessary job skills and by using tests and other screening devices to hire people with those skills.

## 1.9 OPEN FLEXIBLE-ADAPTIVE SYSTEM

A system which is interacts freely with its environment, taking input and returning output. An open system is one that interacts with its environment and thus exchanges information, material, or energy with the environment, including random and undefined inputs. Open systems are adaptive in nature as they tend to react with the environment in such a way organizing', in the sense that they change their continued existence. Such systems are 'self organizing', because they change their organization in response to changing conditions. Five important characteristics of open systems can be identified.

1. **Input from outside:** The open systems are self – adjusting and self-regulating. When functioning properly, an open system reaches a steady state or equilibrium.
2. **Entropy or loss of energy:** Any open systems resist entropy by seeking new inputs or modifying the processes to return to a steady state.
3. **Differentiation:** There are specialization of functions and a greater differentiation of their components.
4. **Equifinality:** The term implies that goals are achieved through differing courses of action and a variety of paths. In most systems, there is more of a consensus on goals than on paths to reach the goals.
5. **Increasing:** All dynamic systems tend to run down over time, resulting in open systems have a tendency toward an increasing.

## 1.10 COMPUTER AS CLOSED SYSTEM

A system which cut off from its environment and does not interact with it is known as close system. A closed system is one, which does not interact with its environment. Such systems, in business world, are rare. Thus the systems that are relatively isolated from the environment but not completely closed are termed closed systems. We can define a computer system as a close system in two ways:

1. **Hardware point of view:** If the computer is not connected with internet or other network then it works like a closed system which is a set of different unit works together. In order to carry out any operations the computer organized the task between its various functional units. A block diagram of different close unit of computer is shown in Fig. 1.16.
   - (i) **Input Unit:** Input unit is a device which provides communication between user and computer. Input of any form is first converted into binary electronic signals (0 and 1), which can be understood by CPU. This process is called digitizing.
   - (ii) **Output unit:** The output coming from the CPU and make it understandable by human beings, i.e., graphical, alphanumeric in human language, audio visual.
   - (iii) **Software point of view:** In computing a closed system refers to software which the specifications and detail of implementation (typically source code) are kept secret, as opposed to open source systems.
   - (iv) **Storage unit:** Data has to be fed into the system before the actual processing starts. It is because the processing speed of CPU is very fast. The data has to be provided to CPU with the same speed. That is why

the data is first stored in the storage unit for faster access and processing. Thus storage unit of the computer system is designed to do the above functionality. It provides space for storing data and instructions.

(v) **Central processing unit:** The CPU is also called the brain of the computer. This is because an execution of any task is controlled by the CPU. CPU takes information from the input unit and processes it according to instructions.

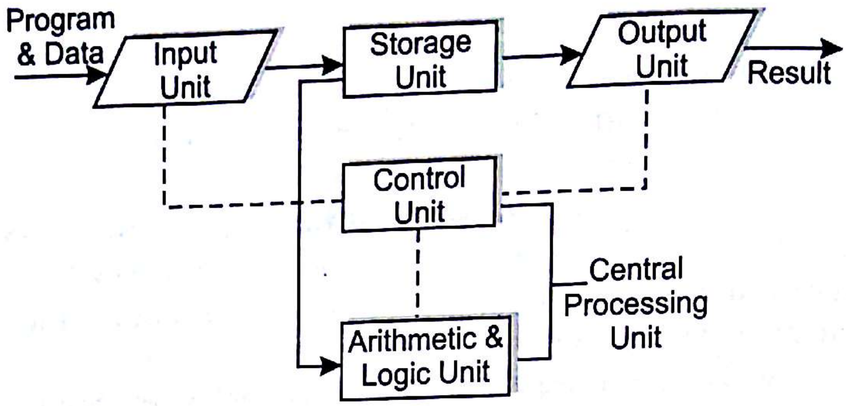


**Fig. 1.16** Different units of system

(vi) **Arithmetical and Logical Unit (ALU):** ALU is designed to perform the four basic arithmetic operations like add, subtract, multiply, divide and logical operations or comparisons such as less than, equal to or greater than. It can do complex calculations with fast speed.

(vii) **Control Unit (CU):** The control unit worked like the supervisor seeing that things are done in proper fashion.

2. **Software point of view:** A computer program is used by associates in a specified department that is not open or shared within the corporate structure. Materials developed for training dedicated associates to handle specific jobs assigned within their department or company. The materials would not be meaningful to anyone outside the assigned area.

## REVIEW QUESTIONS

1. Define system. Explain with a figure and explain the characteristics of systems. *(R.G.P.V., Dec. 2009)*
2. Explain meaning and definition of a "system" and what its major components are.
3. Discuss characteristics of a system.
4. Differentiate between natural and man-made systems. Give four examples. *(R.G.P.V., Dec. 2010)*
5. Explain super and sub systems. What is key component of system? *(R.G.P.V., Dec. 2011)*
6. Explain the following types of system:
   (a) Physical or abstract systems
   (b) Open or closed systems
   (c) Man made information systems
   (d) Formal and informal information system
   (e) Computer based information systems
7. Explain the key component of a system.
8. What is interface? *(R.G.P.V., Dec. 2010)*
9. What do you mean by boundary and interface complexity of system?
10. Explain the open flexible-adaptive system.
11. Explain the computer as closed system.

# 2 System Controlling Coupling and Models

**Chapter Outline**



## 2.1 INTRODUCTION

The managing system must generate at least as much complexity as the system that it is trying to control. If either the managing system or the operational process lacks sufficient complexity then the complexity missed could cause the overall system to fail. A system is a collection of inter-related parts organized for a purpose. Coupling is the description of the extent of the inter-relationship between the parts. A system model is the conceptual model that describes and represents a system. A system comprises multiple views such as planning, requirement (analysis), design, implementation, deployment, structure, behavior, input data, and output data views. A system model is required to describe and represent all these multiple views. The system model describes and represents the multiple views possibly using two different approaches.

## 2.2 LAW OF REQUISITE VARIETY

Variety is the term used in cybernetics to describe complexity. System generates complexity that must try to control.

**Important Point:** *"The law which describes how complexity could operate to overcome a system of management is known as the Law of Requisite Variety."*

The law of requisite variety states that to control a complex system, the managing system must generate at least as much complexity as the system that it is trying to control. If either the managing system or the operational process lacks sufficient complexity then the complexity missed could cause the overall system to fail. In nature this could mean the death of the organism, in business it could mean the death of the organization. Figure 2.1 is a simple representation of the law of requisite variety. The law of requisite variety can be explained as following:

1. **Management:** The figure demonstrates that there is infinite complexity in any environment which management wishes to do business with.
2. **Environment:** The management tried to deal with all the complexity in that environment then it would be overwhelmed. Instead an operational process is designed to interact with the environment, and management interacts with this operational process rather than with the environment itself.

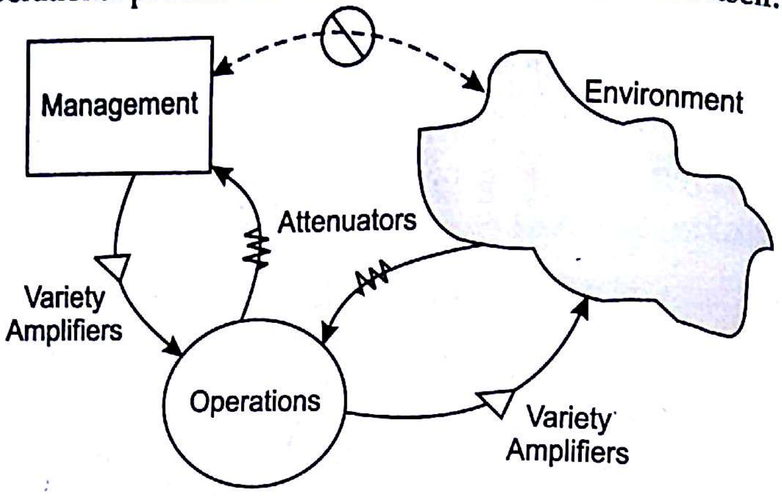


**Fig. 2.1** Law of Requisite Variety

3. **Operations:** The operational process engineers the complexity it faces in the environment by reducing what is receives attenuating complexity away and by increasing the scope of its own interactions with it amplifying the effect of what it does. The same process is repeated for the interactions between management and the operational process.

## 2.3 SYSTEM COUPLING

A system is a collection of inter-related parts organized for a purpose. The design of a system is determined by its couples, not its component parts.

> **Important Point:** *"System coupling is the description of the extent of the inter-relationship between the parts."*

A system is coupled to other systems in a variety of ways. The different types of couples can influence the measure of the performance of the systems.

### 2.3.1 Types of Couples

Couplings occur in a variety of ways through a variety of resources. The different types of couples can influence the measure of the performance of the systems as shown in Fig. 2.2.

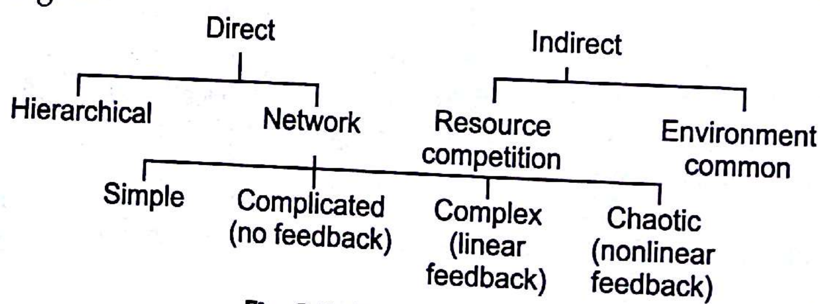


**Fig. 2.2** Types of coupling

1. **Direct coupling**: This direct form of coupling comes in two variants: hierarchical and network.
   (i) **Hierarchical coupling**: A hierarchical coupling occurs within a system, as a form of cohesion. For example, the headquarters of an organization issues orders to supplementary organizations but they cannot issue orders back. They can send information back, in another couple, but the order couple is unidirectional.
   (ii) **Network coupling**: A network coupling occurs between systems at the same hierarchical level. So, the supplementary can communicate with each other. Of course, the headquarters could be part of this network in some designs if there is no central control. They may be in simple, complicated and chaotic.
2. **Indirect coupling**: Another form of indirect coupling occurs when systems are subject to the same pressures from a common environment. Here the measure of acceptability becomes important as if one of these systems does not operate in a way acceptable to the regulators then both systems could be shut down. The indirect coupling comes as:
   (i) **Resource competition**: It can be regarded as coupling the systems through the resource supplier. For example, two systems competing for the same budget are linked through the financial system if they have it in common, as for two parts of the same organization. Perhaps they are coupled through a common creait supplier.

   As described earlier, there can be competition for each of the different types of resources: labour, skills, information (which is not inexhaustible and cost-free to obtain, despite many such assumptions), equipment, space for facilities and of course money. Accordingly there are couples through the source for each of these resources.
   (ii) **Common environment**: Systems coupled by a common environment can be regarded as being linked to the same threat source. The actions of one system in response to the environment influence the other system.

   For example, if one organization decides to react to a credit crunch by raising capital from the stock market then that action takes funds out of the market that other organizations could use or at least raises the price that the other system has to pay for the capital. The market is the system coupled in common to the driving and driven systems.

### 2.3.2 Tight or Loose Coupling

The coupling between systems can range from very tight to very loose.

(i) **Tight coupling**: The coupling is tight if there are many couples between systems, such that the behaviour of one system has a strong and immediate effect upon the behaviour of the coupled system.

(ii) **Loose coupling**: The coupling is loose if the couples are few or not very strong. In this case, it could be some time before the actions of one system flow on to influence the actions of the other system. For example in computing and systems design a loosely coupled system is one in

which each of its components has, or makes use of, little or no knowledge of the definitions of other separate components.

## 2.4 STRESSES AND ENTROPY

The force transmitted by systems' supra-system is known as stresses. It causes system to change. The purpose of stresses enables supra system to better achieve its goals. Each level of system trying to accommodate stress – may impose stress on its sub-system and so on. The impact of stress varies depending on whether a system reacts or does not react to stress as shown in Fig. 2.3.

For example, RBI directive to all member Banks to implement RTGS/cheque transaction. Each Bank's top management passes it on clearing department to modify/upgrade its clearing system. Clearing cell passes it on EDP department to develop new software to suit RTGS.

Entropy prevented through inputs to repair, replenish and maintain systems. Such maintenance inputs are called as "Negative Entropy".

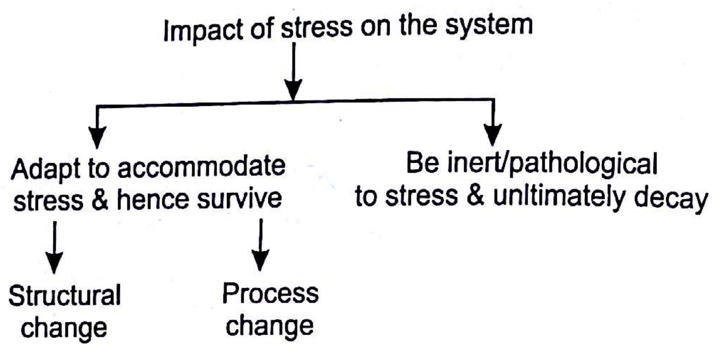


**Fig. 2.3** Impact of stress on the System

## 2.5 FUNCTIONAL & CROSS FUNCTIONAL SYSTEM

1. **Functional system:** The popular functional areas of the business organization are:
   - Human Resource Information System
   - Financial Information System
   - Marketing Information System
   - Production/Marketing Information System

These departments or functions are known as functional areas of business. Each functional area requires applications to perform all information processing related to the function.

**Important Point:** *"The system which is based on the various business functions such as production, marketing, finance and personnel, etc. is called as functional system."*

The functions supported by human resources system is shown in Fig. 2.4.

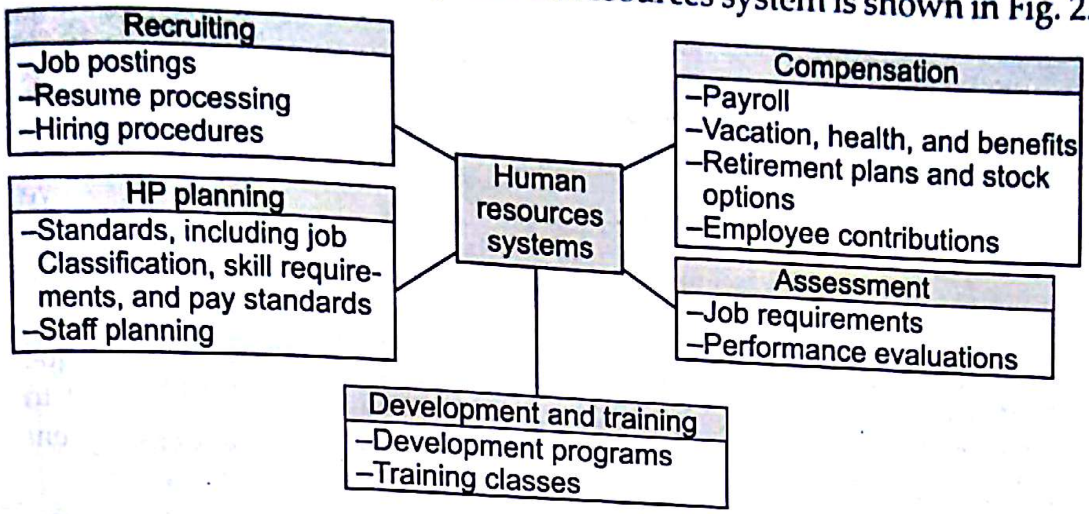


Fig. 2.4 Human Resources System

The function supported by accounting and finance systems is shown in Fig. 2.5.

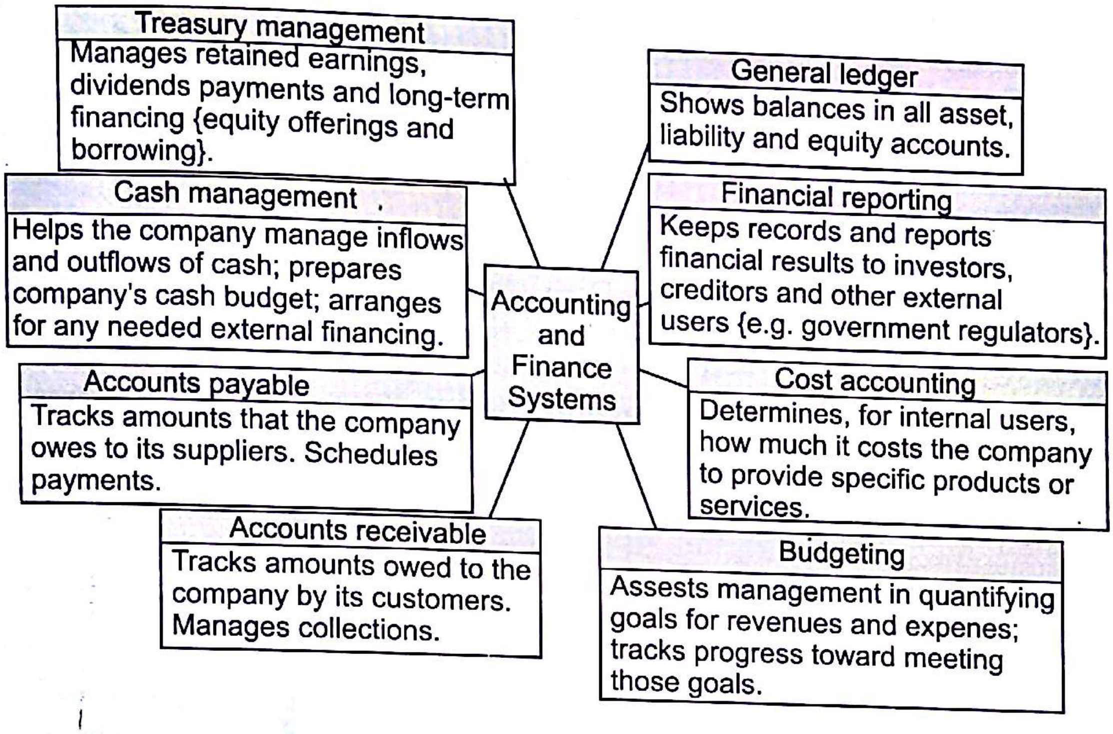


Fig. 2.5 Accounting and Finance Systems

The function supported by Sales and Marketing System is shown in Fig. 2.6.

**Problems of functional systems:**

- Duplicated data: each application with its own database.
- Disjointed business applications.
- Limited information due to lack of integrated enterprise data.
- Inefficient overall activities because of isolated decisions.
- Costly.

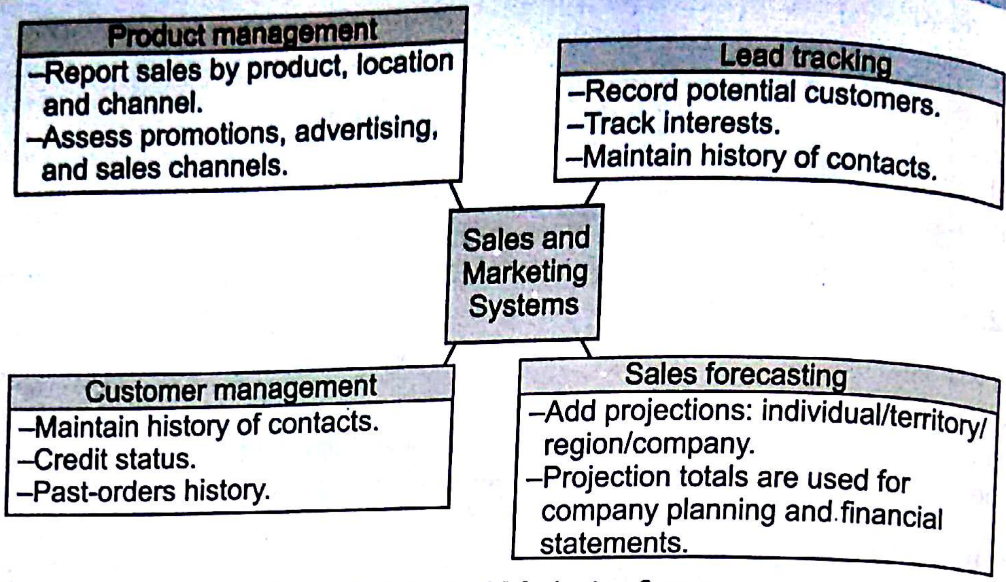


**Fig. 2.6** Sales and Marketing System

2. **Cross functional system:** A cross-functional information system is the third era of information systems, after calculations systems and functional systems. Cross-functional systems were designed to integrate the activities of the entire business process, and are called so because they 'cross' departmental boundaries.

**Important Point:** *"A cross-functional system is a group of people with different functional expertise working toward a common goal. It may include people from finance, marketing, operations, and human resources departments."*

Typically, it includes employees from all levels of an organization. Members may also come from outside an organization (in particular, from suppliers, key customers, or consultants). Such systems support business processes such as: Product development, Production, Distribution, Order management, Customer support, etc. as shown in Fig. 2.7.

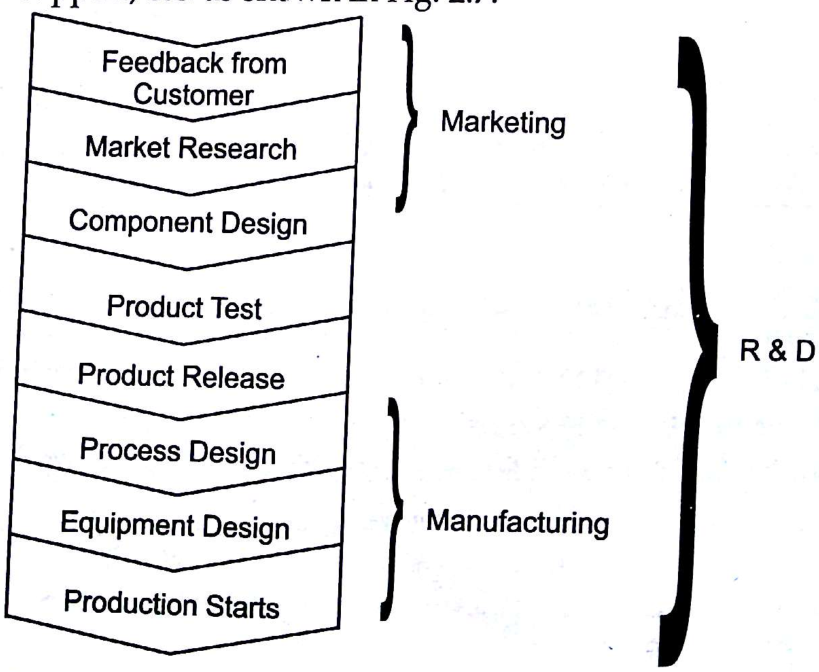


**Fig. 2.7** Business processes

All business processes must be supported by cross-functional information system that crosses the boundaries of several business functions. Many companies are moving one step ahead and trying to install integrated cross-functional client-server applications. They are typically falling in these categories: Enterprise applications integration (EAI), Enterprise resource planning (ERP) and Supply chain management (SCM).

## 2.6 STEVEN ALTARS NINE ELEMENT WORK SYSTEM MODEL

The work system concept is like a common denominator for many of the types of systems that operate within or across organizations. Operational information systems, service systems, projects, supply chains, and ecommerce web sites can all be viewed as special cases of work systems.

**Important Point:** *"A work system is a system in which human participants and/or machines perform work using information, technology, and other resources to produce products and services for internal or external customers."*

Business organizations contain work systems that procure materials from suppliers, produce products, deliver products to customers, find customers, create financial reports, hire employees, coordinate work across departments, and perform many other functions. The work system approach contains two central frameworks.

- Nine elements of the work system
- Work system life cycle model

## 2.7 NINE ELEMENTS OF THE WORK SYSTEM

The nine elements of the work system framework as shown in Fig. 2.8 are the basis for describing and analyzing an IT-reliant work system in an organization. The framework outlines a static view of a work systems form and function at a point in time and is designed to emphasize business rather than IT concerns. 2.8 say that work systems exist to produce products and services for customers. The arrows say that the elements of a work system should be in alignment.

1. **Processes and activities:** It includes everything that happens within the work system. The term processes and activities is used instead of the term business process because many work systems do not contain highly structured business processes involving a prescribed sequence of steps, each of which is triggered in a pre-defined manner. Other perspectives with their own valuable concepts and terminology include decision-making, communication, coordination, control, and information processing.
2. **Participants:** They are people who perform the work. Some may use computers and IT extensively, whereas others may use little or no technology. When analyzing a work system the more encompassing role of work system participant is more important than the more limited role of technology user.

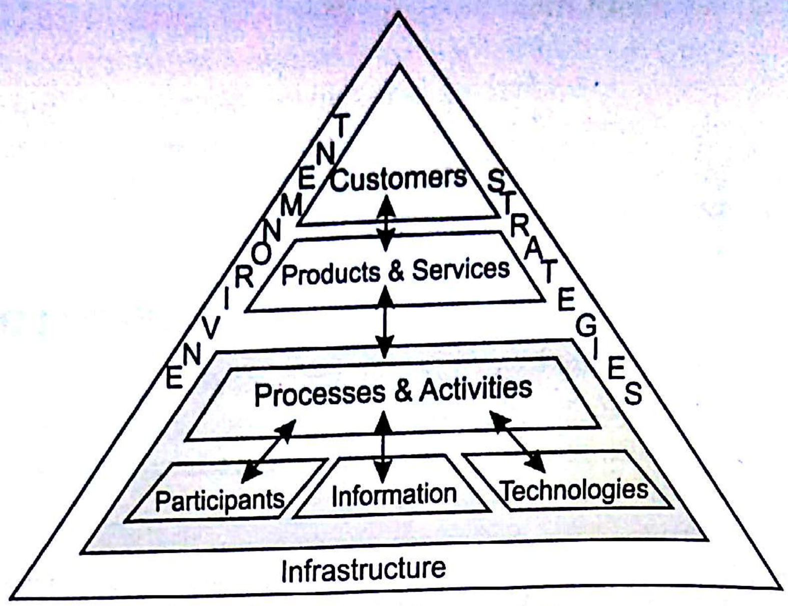


Fig. 2.8 Work System Framework

3. **Information**: It includes codified and non-codified information used and created as participants perform their work. Information may or may not be computerized.
4. **Technologies**: It includes tools such as cell phones, projectors, spreadsheet software, and automobiles and techniques such as management by objectives, optimization, and remote tracking that work system participants use while doing their work.
5. **Products and services**: These are the combination of physical things, information, and services that the work system produces. This may include physical products, information products, services, intangibles such as enjoyment and peace of mind, and social products such as arrangements, agreements, and organizations.
6. **Customers**: These are people who receive direct benefit from products and services the work system produces. They include external customers who receive the organization's products and/or services and internal customers who are employees or contractors working inside the organization.
7. **Environment**: It includes the organizational, cultural, competitive, technical, and regulatory environment within which the work system operates.
8. **Infrastructure**: It includes human, informational, and technical resources that the work system relies on even though these resources exist and are managed outside of it and are shared with other work systems.
9. **Strategies**: It includes the strategies of the work system and of the department(s) and enterprise(s) within which the work system exists. Strategies at the department and enterprise level may help in explaining why the work system operates as it does and whether it is operating properly.

## 2.8 WORK SYSTEM LIFE CYCLE MODEL (WSLC)

The other central framework in the work system approach is the work system life cycle model as shown in Fig. 2.9 which expresses a dynamic view of how work

systems change over time through iterations involving planned and unplanned change.

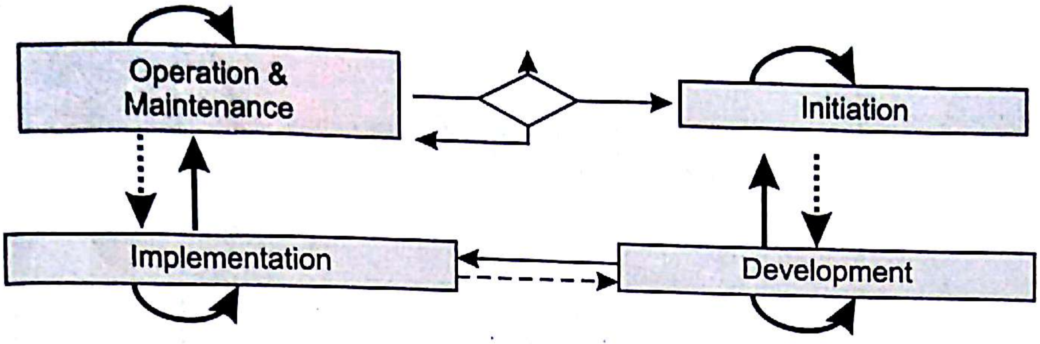


Fig. 2.9 Work System Life Cycle Model

The WSLC differs fundamentally from the "System Development Life Cycle (SDLC)."

(i) **First,** the SDLC is basically a project model rather than a system life cycle. Some current versions of the SDLC contain iterations, but even those are basically iterations within a project.

(ii) **Second,** the system in the SDLC is a basically a technical artifact that is being programmed. In contrast, the system in the WSLC is a work system that evolves over time through multiple iterations. This evolution occurs through a combination of defined projects and incremental changes resulting from small adaptations and experimentation. In contrast with control-oriented versions of the SDLC, the WSLC treats unplanned changes as part of a work systems natural evolution.

## 2.9 IPO (Input-Processing-Output) MODEL

In response to the changing background of organizations driven by computer systems, Input-Process-Output (IPO) Model was proposed.

**Important Point:** *"IPO Model states that the outcome of a meeting depends on the process that occurs during the meeting, which is in turn dependent on what is put into the meeting."*

The Fig. 2.10 demonstrates how resources put into the system (inputs) undergo a change (process) to produce results (outputs).

1. **Input:** The sources are flowing into the system. These sources can include knowledge, attitudes, behaviors, resources and technology.
2. **Process:** The action is of changing the input.
3. **Output:** The result is flowing out of the system.

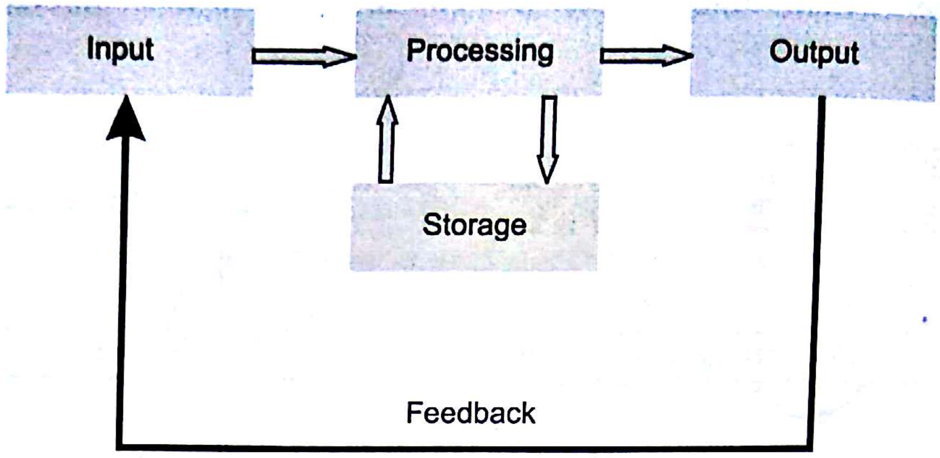


Fig. 2.10 Input-Processing-Output Model

4. **Storage:** Location is where material inside the system is placed for possible use at a later point in time.
5. **Feedback:** This occurs when the outcome has an influence on the input.
   The goal of the IPO model is to maximize process gains (actions during the process phase that improves output) while minimizing process losses (actions during the process phase that impairs output).

## 2.10 STRUCTURE AND PERFORMANCE OF WORK SYSTEMS LEADING TO CUSTOMER DELIGHT

High performance work systems (HPWS) are organizations that utilize a fundamentally different approach to managing than the traditional hierarchical approach associated with mass production/scientific management. At the heart of this emerging approach is a radically different employer-employee relationship. Leading organizational behaviour specialists believe that HPWS has the greatest potential to provide sustained competitive advantage to companies adopting it.

**Important Point:** *"High-performance work system is a right combination of people, technology, and organizational structure that makes full use of the organization resources and opportunities in achieving its goals."*

To function as a high-performance work system, each of these elements must fit well with the others in a smoothly functioning whole.

### 2.10.1 Structure of a High-Performance Work System

The element of high performs work system as shown in Fig. 2.11 are as following:

1. **Organizational structure:** The way the organization groups its people into useful divisions, departments, and reporting relationships. For example, the hierarchical relationships starting with the president on top and leading downward to the blue – collar workers represents the organization structure as shown in Fig. 2.11.

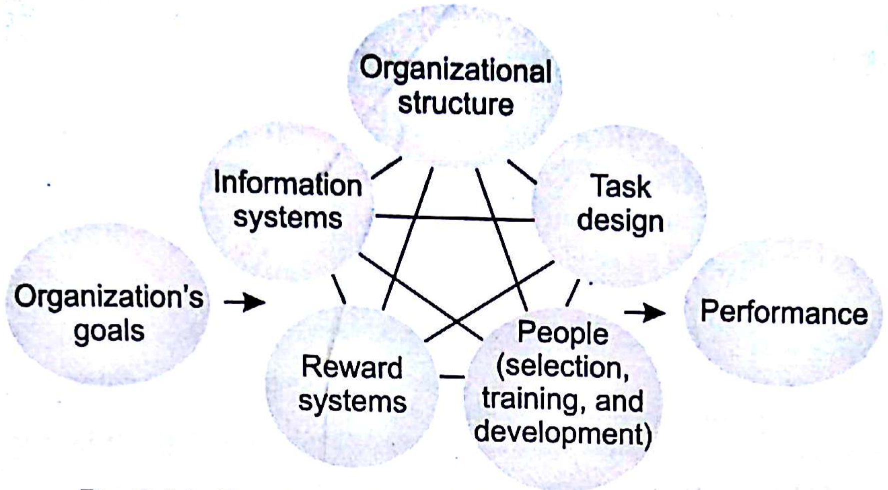


Fig. 2.11 Structure of a High-Performance Work System

2. **Task design:** Determines how the details of the organization necessary activities will be grouped whether into jobs or team responsibilities.
3. **People:** It is well suited and well prepared for their jobs.
4. **Reward systems:** Contribute to high performance by encouraging people to strive for objectives that support the organizations overall goals.
5. **Information systems:** Modern information systems have enabled organizations to share information widely.

### 2.10.2 Performance of Work Systems

The outcomes of each employee and work group contribute to the system overall performance.

The organizations individuals and groups works efficiently, provide high-quality goods and services, etc., and in this way they contribute to meeting the organizations goals. Outcomes of a High-Performance Work System are shown in Fig. 2.12.

When the organization adds or changes goals, people are flexible and make changes to as needed to meet the new goals. Teams perform work and employees participate in selection. Employees receive formal performance feedback and are

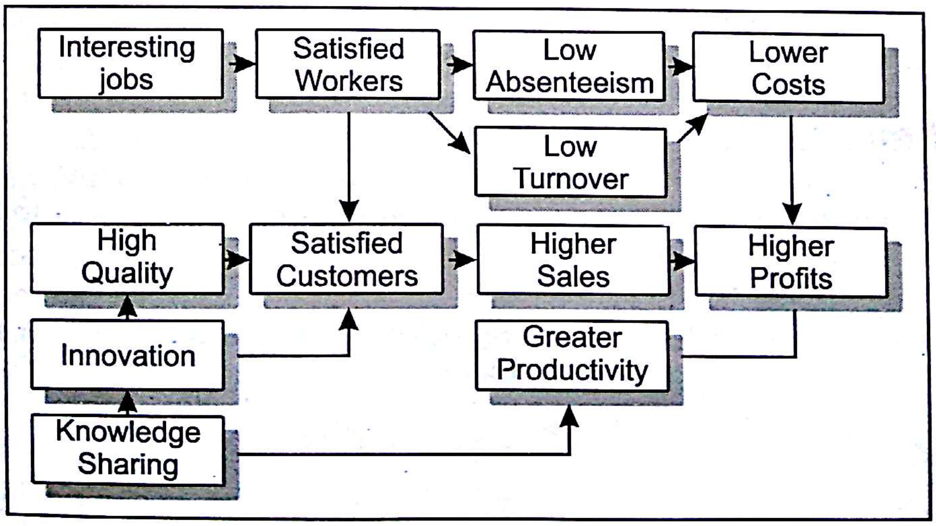


Fig.2.12 High Performance of Work Systems

actively involved in the performance improvement process. Ongoing training is emphasized and rewarded. Employee's rewards and compensation related to the company's financial performance.

Equipment and work processes are structured and technology is used to encourage maximum flexibility and interaction among employees. Employees participate in planning changes in equipment, layout, and work methods. Work design allows employees to use a variety of skills.

## REVIEW QUESTIONS

1. Explain feedback /pull control in a system. *(R.G.P.V., Dec. 2009)*
2. Draw Steven alters' nine element work system model. *(R.G.P.V., Dec. 2009)*
3. Discuss input-processing-output model open organization viewed as a system.
4. What are system coupling and its various types?
5. Explain feed forward /push control in a system. *(R.G.P.V., Dec. 2009, Dec. 2012)*
6. Explain whether computer is an open or closed system. *(R.G.P.V., Dec. 2010)*
7. What is law of requisite variety and its implications?
8. What is functional and cross functional system?
9. Explain steven altars nine element work system model.
10. Discuss structure and performance of work systems leading to customer delight.

# 3 Management Roles and Functions

## Chapter Outline

- Introduction
- Meaning and Definition
- Functions of Management
- Importance of Management
- Schools of Theories
  - ⇒ Classical School of Management (Administrative Management)
  - ⇒ Bureaucratic Management
  - ⇒ Classical School of Management
- Hawthorne Experiments
- Knowledge Driven Learning Organization
- E-Business/E-Commerce
  - ⇒ Benefits of E-Commerce
  - ⇒ Application of E-Commerce

## 3.1 INTRODUCTION

Management in all business and organizational activities is the act of getting people together to accomplish desired goals and objectives using available resources efficiently and effectively. Management comprises planning, organizing, staffing, leading or directing and controlling an organization or effort for the purpose of accomplishing a goal. Resourcing encompasses the deployment and manipulation of human resources, financial resources, technological resources and natural resources. Since organizations can be viewed as systems, management can also be defined as human action, including design, to facilitate the production of useful outcomes from a system. This view opens the opportunity to manage oneself, a pre-requisite to attempting to manage others.

## 3.2 MEANING AND DEFINITION

Management is the process of reaching organizational goals by working with and through people and other organizational resources. It is a dynamic process consisting of various elements and activities. These activities are different from operative functions like marketing, finance, purchase etc. Rather these activities are common to each and every manager irrespective of his level or status. The definitions by some of the leading management thinkers and practitioners are given below:

**Important Point:** *"There are four fundamental functions of management i.e., planning, organizing, actuating and controlling".*

*George & Jerry,*

*"Management is principally the task of planning, co-ordinating, motivating and controlling the efforts of others towards a specific objective."*

*—James L. Lundy*

*"To manage is to forecast and plan, to organize, to command and to control".*

*—Henry Fayol*

*Management is the art and science of organizing and directing human efforts applied to control the forces and utilize the materials of nature for the benefit of man.*

*—American Society of Mechanical Engineers*

*Management is guiding human and physical resources into dynamic organizational units which attain their objectives to the satisfaction of those served and with a high degree of morale and sense of attainment on the part of those rendering service.*

*—American Management Association*

From the above definitions management has the following three characteristics:

1. It is a process or series of continuing and related activities.
2. It involves and concentrates on reaching organizational goals.
3. It reaches these goals by working with and through people and other organizational resources.

## 3.3 FUNCTIONS OF MANAGEMENT

There are five basic management functions that make up the management process as described in the following sections shown in Fig. 3.1:

1. **Planning**: Planning activity focuses on attaining goals. Managers outline exactly what organizations should do to be successful.

**Important Point**: *"Planning involves choosing tasks that must be performed to attain organizational goals, outlining how the tasks must be performed, and indicating when they should be performed."*

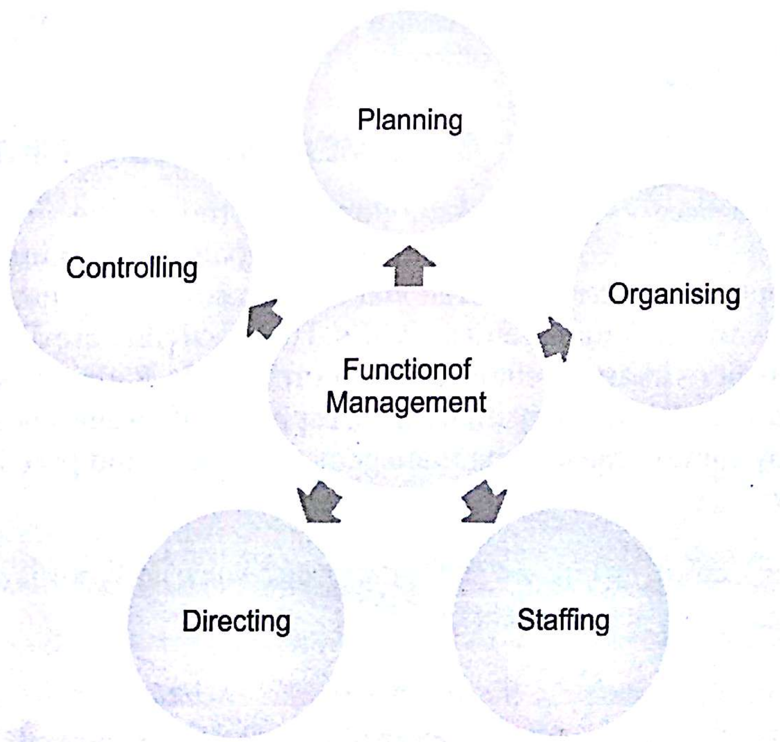


**Fig. 3.1** Functions of Management

Planning is concerned with the success of the organization in the short term as well as in the long term. Organizing as a process involves:

- It is making decisions on future course of actions.
- It involves taking decisions on vision, mission, values, objectives, strategies and policies of an organization.
- It is done for immediate, short term, medium term and long term periods.
- It is a guideline for execution/implementation.
- It is a measure to check the effectiveness and efficient of an organization.

2. **Organizing:** This can be thought of as assigning the tasks developed in the planning stages, to various individuals or groups within the organization.

**Important Point:** *"Organizing is to create a mechanism to put plans into action. People within the organization are given work assignments that contribute to the company's goals."*

Tasks are organized so that the output of each individual contribution to the success of departments, which, in turn, contributes to the success of divisions, which ultimately contributes to the success of the organization. Organizing as a process involves:

- Identification of activities.
- Classification of grouping of activities.
- Assignment of duties.
- Delegation of authority and creation of responsibility.
- Co-ordinating authority and responsibility relationships.

3. **Staffing:** It is the function of managing the organization structure and keeping it manned. Staffing has assumed greater importance in the recent years due to advancement of technology, increase in size of business, complexity of human behavior, etc.

**Important Point:** *"Managerial function of staffing involves managing the organization structure through proper and effective selection, appraisal and development of personnel to fill the roles designed in the structure".* *-Kootz and O'Donell,*

**Staffing involves:**

- It includes manpower or human resource planning.
- Staffing involves recruitment, selection, induction and positioning the people in the organization.
- Decisions on remuneration packages are part of staffing.
- Training, re-training, development, mentoring and counselling are important aspects of staffing.
- It also includes performance appraisals and designing and administering the motivational packages.

4. **Directing:** Communicate and co-ordinate with people to lead and ensure them to work effectively together to achieve the plans of the organization.

**Important Point:** *"Directing includes leading, motivating, communicating and coordinating."*

**It includes:**

- It is one of the most important functions of management to translate company's plan into execution.
- It includes providing leadership to people so that they work willingly and enthusiastically.
- Directing people involves motivating them all the time to create zeal among them to give their best.
- Communicating companies' plan throughout the organization is an important directing activity.
- It also means co-ordinating various people and their activities.
- Directing aims at achieving the best not just out of an individual but achieving the best through the group or team of people through team building efforts.

5. **Controlling:** Controlling also requires a plan and a clear organization structure. The control process is used for establishing standards, correcting deviations, if any, measuring performance and establishing standards.

**Important Point:** *"This involves measuring and correcting the performance of the activities of subordinates so that the defined objectives and the plans devised to achieve those moves in the right direction."*

**Thus:**

- It includes verifying the actual execution against the plans to ensure that execution is being done in accordance with the plans.
- It measures actual performance against the plans.
- It set standards or norms of performance.
- It measures the effective and efficiency of execution against these standards and the plans.
- It periodically reviews, evaluates and monitors the performance.
- If the gaps are found between execution levels and the plans, controlling function involves suitable corrective actions to expedite the execution to match up with the plans or in certain circumstances deciding to make modifications in the plans.

## 3.4 IMPORTANCE OF MANAGEMENT

All organizations depend upon group efforts. Group action and joint efforts have become necessary in every walk of life. Management is required wherever two or more people work together to achieve common objectives. The success in group efforts depend upon mutual co-operation among the members of the group. Management creates teamwork and co-ordination among specialized efforts. Management is indispensable in all organizations whether a business firm, a government, a hospital, a college, a club, and even in informal group. Management is a creative force which helps in the optimum utilization of resources.

1. **Achieving group goals:** It arranges the factors of production, assembles and organizes the resources, integrates the resources in effective manner to achieve goals. It directs group efforts towards achievement of pre-determined goals.

By defining objective of organization clearly there would be no wastage of time, money and effort. Management converts disorganized resources of men, machines, money, etc. into useful enterprise. These resources are coordinated, directed and controlled in such a manner that enterprise work towards attainment of goals.

2. **Minimization of cost**: In the modern era of cut-throat competition no business can succeed unless it is able to supply the required goods and services at the lowest possible cost per unit. Management directs day-to-day operations in such a manner that all wastage and extravagance are avoided. By reducing costs and improving efficiency, managers enable an enterprise to be competent to face competitors and earn profits.
3. **Encourages Innovation**: Management also encourages innovation in the organization. Innovation brings new ideas, new technology, new methods, new products, new services, etc. This makes the organization more competitive and efficient.
4. **Generation of employment**: By setting up and expanding business enterprises, managers create jobs for the people. People earn their livelihood by working in these organizations. Managers also create such an environment that people working in enterprise can get job satisfaction and happiness. In this way managers help to satisfy the economic and social needs of the employees.
5. **Improves standard of living**: Efficient management leads to better economical production which in turm increases the welfare of people. Good management makes a difficult task easier by avoiding wastage of scarce resource. It improves standard of living. It increases the profit which is beneficial to business and society will get maximum output at minimum cost by creating employment opportunities which generate income in hands. Organization comes with new products and researches beneficial for society.
6. **Development of the nation**: Efficient management is equally important at the national level. Management is the most crucial factor in economic and social development. The development of a country largely depends on the quality of the management of its resources.

## 3.5 SCHOOLS OF THEORIES

Management theories are the set of general rules that guide the managers to manage an organization. Theories are an explanation to assist employees to effectively relate to the business goals and implement effective means to achieve the same.

1. **Administrative Management (Classical School of Management)**: Administrative management basically focuses on how a business should be organized and the practices an effective manager should follow. While pioneer of scientific management tried to determine the best way to perform a job, those in the administrative management explored the possibilities of an ideal way (rule of thumb) to put all jobs together and operate an organization. Thus the main focus of administrative school or general management theory is on finding "the best way" to run organizations. Administrative management school is also called "traditional principles of management". **Henry Fayol**, a French industrialist, the chief architect and the father of the administrative

management theory. According to Fayol the five functions of managers were as shown in Fig. 3.2:

**(i) Planning**: It is drawing up plans of actions that combine unity, continuity, flexibility and precision given the organization's resources, type and significance of work and future trends. Creating a plan of action is the most difficult of the five tasks and requires the active participation of the entire organization. Planning must be co-ordinated on different levels and with different time horizons.

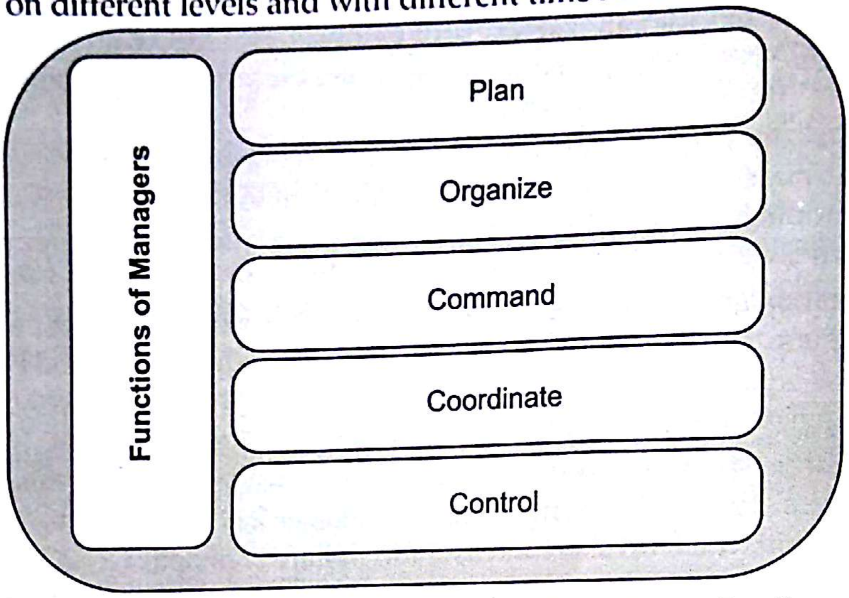


**Fig. 3.2** Functions of Managers (According to Henry Fayol)

**(ii) Organizing**: It providing capital, personnel and raw materials for the day-to-day running of the business, and building a structure to match the work. Organizational structure depends entirely on the number of employees. An increase in the number of functions expands the organization horizontally and promotes additional layers of supervision.

**(iii) Commanding**: It is optimizing return from all employees in the interest of the entire enterprise. Successful managers have personal integrity, communicate clearly and base their judgments on regular audits. Their thorough knowledge of personnel creates unity, energy, initiative and loyalty and eliminates incompetence.

**(iv) Co-ordinating**: This is unifying and harmonizing activities and efforts to maintain the balance between the activities of the organization as in sales to production and procurement to production. Fayol recommended weekly conferences for department heads to solve problems of common interest.

Fayol concluded that all activities that occur in business organizations could be divided into six main groups and all the following activities are interdependent:

1. Technical (production, manufacturing)
2. Commercial (buying, selling, exchange)
3. Financial (obtaining and using capital)
4. Security (protection of property and persons)
5. Accounting (balance sheet, stocktaking, costing)
6. Managerial (planning, organizing, commanding, coordinating, controlling).

2. **Bureaucratic Management:** Max Weber embellished the scientific management theory with his bureaucratic management theory which is mainly focused on dividing organizations into hierarchies, establishing strong lines of authority and control.

**Importacnt Point:** *"Bureaucratic management may be described as "a formal system of organisation based on clearly defined hierarchical levels and roles in order to maintain efficiency and effectiveness."*

Weber suggested organizations develop comprehensive and detailed standard operating procedures for all routines tasks. Bureaucratic structures evolved from traditional structures with the following changes:

1. Jurisdictional areas are clearly specified, activities are distributed as official duties (unlike traditional form where duties delegated by leader and changed at any time).
2. Organization follows hierarchical principle -- subordinates follow orders of superiors, but have right of appeal (in contrast to more diffuse structure in traditional authority).
3. Intention, abstract rules govern decisions and actions. Rules are stable, exhaustive, and can be learned. Decisions are recorded in permanent files (in traditional forms few explicit rules or written records).
4. Means of production or administration belong to office. Personal property separated from office property.
5. Officials are selected on basis of technical qualifications, appointed and not elected, and compensated by salary.
6. Employment by the organization is a career. The official is a full-time employee and looks forward to a life-long career. After a trial period they get tenure of position and are protected from arbitrary dismissal.

3. **The Classical School of Management:** The classical school is the oldest formal school of management thought. Its roots pre-date the twentieth century. The classical school of thought generally concerns ways to manage work and organizations more efficiently. Three areas of study that can be grouped under the classical school are scientific management, administrative management, and bureaucratic management. The classical school of management has sought to define the essence of management in the form of universal fundamental functions. These, it was hoped, would form the cognitive basis for a set of relevant skills to be acquired, by all would-be managers through formal education.

   Fayol is the representative of classical school of management thought. Administrative management is the managerial mode he stood for where it applied essential points to administrative management principles of controllers.

**Importacnt Point:** *Fayol's famous works: Industrial management and common management. He divided management into five segments. Therefore, it denoted controllers were to carry out the five segments, i.e. to forecast, to organize, to command, to coordinate, to control. By now, these five segments are still the functional basis and basic process by which controller's research into management.*

According to his thought over management, therefore, 14 principles of organization came into existence. These 14 universal principles of organization are:

1. **Division of work:** Professionally increased output is done through improving effectiveness of the workers.
2. **Authority:** The managers were required to be good at giving commands as authority conferred them right to do so but responsibility were accompanying authority.
3. **Discipline:** The workers must adhere to and respect organizational rules and regulations. The managers and workers must have clear understanding towards organizational rules and regulations. Organization must enforce effective sanction upon those workers who broke organizational rules and regulations.
4. **Interests of the individual should subordinate to interests of the collective:** Interests of any individuals or groups should not exceed organizational interest as the collective.
5. **Remuneration:** It was required to improve the workers jobs and offer equal wages treatment.
6. **Concentration of power:** It refers the level of the workers involvement in decision-making.
7. **Scalar chain:** The establishment of a line of authority by which communication must comply with the chain by levels of authority from the seniors to the subordinate.
8. **Order:** The workers and substance should be on the corresponding position at appropriate time.
9. **Equality:** Managers ought to keep kindness and equality for the workers.
10. **Stability of employees:** The terms of office as high mobile or higher turnover of labours would lead to low effectiveness and efficiency.
11. **Initiative:** When being allowed to participate in formulation and enforcement of planning, employees would complete works with their great efforts.
13. **Right substitute as positions:** High mobile labour would lead to low effectiveness. The managers should formulate plans of human affairs in order as to find the right substitute as positions appeared vacant.
14. **Esprit de corps (sense of belonging/part of team):** It publicized that esprit de corps would be established and unified harmoniously.

## 3.6 HAWTHORNE EXPERIMENTS

The Hawthorne experiments were ground breaking studies in human relations that were conducted between 1924 and 1932 at Western Electric Company's Hawthorne Works in Chicago. The Hawthorne effect is a psychological phenomenon that produces an improvement in human behaviour or performance as a result of increased attention from superiors, clients or colleagues. In a collaborative effort, the effect can enhance results by creating a sense of teamwork and common purpose.

**Elton Mayo's** studies grew out of preliminary experiments at the Hawthorne plant from 1924 to 1927 on the effect of light on productivity. Those experiments

showed no clear connection between productivity and the amount of illumination but researchers began to wonder what kind of changes would influence output.

1. **Variables affecting productivity:** Specifically, Elton Mayo wanted to find out what effect fatigue and monotony had on job productivity and how to control them through such variables as rest breaks, work hours, temperature and humidity. In the process, he stumbled upon a principle of human motivation that would help to revolutionize the theory and practice of management. Elton Mayo selected two women, and had those two select an additional four from the assembly line, segregated them from the rest of the factory and put them under the eye of a supervisor who was more a friendly observer than disciplinarian. Mayo made frequent changes in their working conditions, always discussing and explaining the changes in advance.
2. **Relay Assembly:** The group was employed in assembling telephone relays-a relay being a small but complicated mechanism composed of about forty separate parts which had to be assembled by the girls seated at alone bench and dropped into a shaft when completed. The relays were mechanically counted as they slipped down the shaft. The intent was to measure the basic rate of production before making any environmental changes. Then, as changes were introduced, the impact to effectiveness would be measured by increased or decreased production of the relays.
3. **Feedback mechanism:** Throughout the series of experiments, an observer sat with the girls in the workshop noting all that went on, keeping the girls informed about the experiment, asking for advice or information, and listening to their complaints. The experiment began by introducing various changes, each of which was continued for a test period of four to twelve weeks. The results of these changes are as follows:

### 3.6.1 Work Conditions and Productivity

1. Work is a group activity, team work can increase a worker's motivation as it allows people to form strong working relationships and increases trust between the workers.
2. Work groups are created formally by the employer but also occur informally. Both informal and formal groups should be used to increase productivity as informal groups influence the worker's habits and attitudes.
3. Workers are motivated by the social aspect of work, as demonstrated by the female workers socializing during and outside work and the subsequent increase in motivation.
4. Workers are motivated by recognition, security and a sense of belonging.
5. The communication between workers and management influences workers' morale and productivity. Workers are motivated through a good working relationship with management.

## 3.7 KNOWLEDGE DRIVEN LEARNING ORGANIZATION

Knowledge driven learning organization is one of the most recent topics today in both the industry world and information research world. In our daily life, we deal with huge amount of data and information. Data and information is not knowledge

until we know, how to dig the value out of it. This is the reason we need knowledge management. Unfortunately, there's no universal definition of knowledge management, just as there's no agreement as to what constitutes knowledge in the first place. We chose the following definition for knowledge management for its simplicity and broad context.

**Importacnt Point:** *"Knowledge Management (KM) refers to a multi-disciplined approach to achieve organizational objectives by making the best use of knowledge. KM focuses on processes such as acquiring, creating and sharing knowledge and the cultural and technical foundations that support them."*

Knowledge management draws from a wide range of disciplines and technologies:

1. Cognitive science
2. Expert systems, artificial intelligence and knowledge base management systems (KBMS)
3. Computer-supported collaborative work (group-ware)
4. Library and information science
5. Technical writing
6. Document management
7. Decision support systems
8. Semantic networks
9. Relational and object databases
10. Simulation
11. Organizational science
12. Object-oriented information modeling
13. Electronic publishing technology, hypertext, and the World Wide Web (www); help-desk technology
14. Full-text search and retrieval
15. Performance support systems

The main drivers behind knowledge management efforts are:

1. **Knowledge Attrition**: Despite the economic slowdown, voluntary employee turnover remains high.
2. **Knowledge Merging**: The recent passion of corporate mergers coupled with the increased need to integrate global corporate communications requires the merging of disparate and often conflicting knowledge models.
3. **Content Management**: The explosion of digitally stored business-critical data is widely documented.
4. **E-Learning**: As the economy becomes more global and the use of PCs more pervasive, there has been a dramatic increase in e-learning, also known as computer based training. E-learning is closely linked to an overlapping with, but not equal to knowledge management. E-learning can be an effective medium for knowledge management deliverables.

## 3.8 E-BUSINESS/E-COMMERCE

Electronic commerce is also known as e-commerce or e-business. Trade and commerce between individuals is as old as the existence of mankind. The latest to join the list is electronic commerce, which is popularly known as e-commerce. Electronic commerce is defined as the actual buying and selling of goods or services electronically on line. Products are displayed in an on-line store and potential customers can read information about the products see them on the website and have the option to purchase them online. Any product can be sold online and all the principles of business apply to this also. The important requirements to conduct the e-commerce business are as follows:

(a) Website either owned or supplied by cart provider.

(b) A shopping cart programme to list out product or services and means to collect purchaser information.

(c) A method to get the funds into the bank account.

**Importacnt Point:** *E-commerce is a system that consists of the buying and selling of products or services over electronic systems such as the Internet and other computer networks.*

The amount of trade conducted electronically with widespread internet usage. The use of commerce is conducted in this way, encouraging and drawing on innovations in electronic funds transfer, supply chain management, internet marketing, online transaction processing (as shown in Fig. 3.3), electronic data interchange (EDI), inventory management systems, and automated data collection systems. Modern electronic commerce typically uses the World Wide Web at least at some point in the transaction's lifecycle, although it can encompass a wider range of technologies such as e-mail as well.

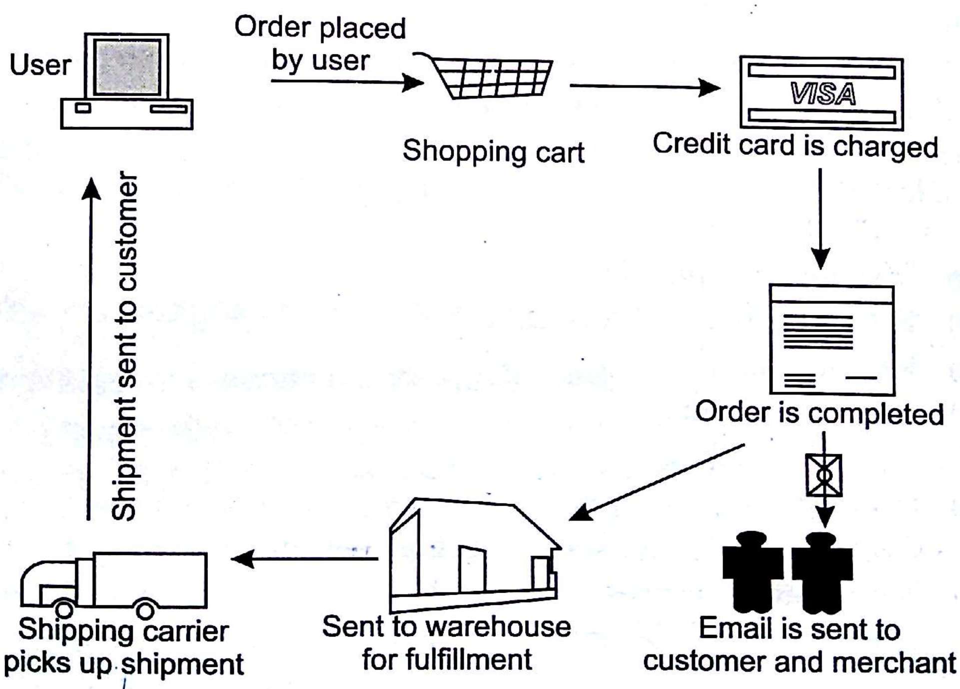


**Fig. 3.3 E-Commerce**

### 3.8.1 Benefits of E-Commerce

The benefits of e-commerce are as following:

1. **Save time**: Ecommerce allows people to carry out businesses without the barriers of time or distance. One can log on to the internet at any point of time, be it day or night and purchase or sell anything one desires at a single click of the mouse.
2. **Low cost**: The direct cost-of-sale for an order taken from a website is lower than through traditional means (retail, paper based), as there is no human interaction during the on-line electronic purchase order process. Also, electronic selling virtually eliminates processing errors, as well as being faster and more convenient for the visitor.
3. **Vast market**: E-commerce is ideal for niche products. Customers for such products are usually few. But in the vast market place i.e., the internet, even niche products could generate viable volumes.
4. **Cheapest**: Another important benefit of e-commerce is that it is the cheapest means of doing business.
5. **Competitions**: The day-to-day pressures of the marketplace have played their part in reducing the opportunities for companies to invest in improving their competitive position. A mature market, increased competitions have all reduced the amount of money available to invest. If the selling price cannot be increased and the manufactured cost cannot be decreased then the difference can be in the way the business is carried out. E-commerce has provided the solution by decimating the costs, which are incurred.
6. **Tangible benefits**: From the buyer's perspective also e-commerce offers a lot of tangible advantages.
   (a) Reduction in buyer's sorting out time.
   (b) Better buyer decisions.
   (c) Less time is spent in resolving invoice and order discrepancies.
   (d) Increased opportunities for buying alternative products.
7. **Strategic benefits**: The strategic benefit of making a business 'e-commerce enabled', is that it helps reduce the delivery time, labour cost and the cost incurred in the following areas:
   (a) Document preparation.
   (b) Error detection and correction.
   (c) Reconciliation.
   (d) Mail preparation.
   (e) Telephone calling.
   (f) Data entry.
   (g) Overtime.
   (h) Supervision expenses.
8. **Operational benefits**: Operational benefits of e-commerce include reducing both the time and personnel required to complete business processes and reducing strain on other resources. It's because of all these advantages that one can harness the power of e-commerce and convert a business to e-business

by using powerful turnkey e-commerce solutions made available by e-business solution providers.

### 3.8.2 Application of E-Commerce

Today e-commerce is being used in different fields, which are as under:

1. **Transaction Processing System:** All data, which comes under any sort of transaction, make use of e-commerce like – airline/railway/hotels reservation, stock trading, insurance policy, etc.
2. **Education and Medical:** Today e-commerce is playing a vital role in improving the technologies used in education and medical department. There are many different online facilities, which allow the users to collect information regarding this field.
3. **Information Services:** There are many different information services available today like - American online, which helps in gathering latest information.
4. **Value Aided Network:** With this facility the business information are being converted from one network to other network.
5. **Electronic Payment:** Today anyone having the ATM (Automatic Teller Machine), internet banking or credit cards can be directly involved in the transaction of many. It is one of the latest technologies, which allows the users to freely perform the marketing jobs.

### 3.8.3 Advantages of E-Commerce

The advantages of e-commerce are as following:

1. It is very easy to reach the customers throughout the world at any time via internet or via an electronic data interchange (EDI) system.
2. Throughout the year, on all the days this system can be operated.
3. The cost of setting up of an e-commerce website is very low when compared with retail outlet.
4. There is more flexibility in a website to add and remove a product than in catalogues or brochures.
5. It potentially gives exposure to previously untapped market segments.
6. It offers wide choice and wastage of time can be avoided.

### 3.8.4 Disadvantages of E-Commerce

The disadvantages of e-commerce are as following:

1. There is no possibility to touch and feel merchandise.
2. With growing importance of e-commerce and computer communication technologies the social contacts of the consumers are going to be reduced.
3. Since online stores do not exist for long periods, many companies do not know exactly the set-up of store.
4. There is a possibility for intercepting transactions and cause problems to consumers and companies who operate on the internet.

## 3.9 UNCERTAINTY AND ADAPTABILITY

**Uncertainty** is applied to predictions of future events, to physical measurements already made, or to the unknown. Although the terms are used in various ways among the general public, many specialists in decision theory, statistics and other quantitative fields have defined uncertainty, risk, and their measurement as:

1. **Uncertainty**: It refers to the lack of certainty. It is a state of having limited knowledge where it is impossible to exactly describe the existing state, a future outcome, or more than one possible outcome.
2. **Measurement of Uncertainty**: A set of possible states or outcomes where probabilities are assigned to each possible state or outcome– this also includes the application of a probability density function to continuous variables and expected value or outcomes can be calculated.
3. **Risk**: It is a state of uncertainty where some possible outcomes have an undesired effect, results or significant loss.
4. **Measurement of Risk**: A set of measured uncertainties where some possible outcomes are losses, and the magnitudes of those losses – this also includes loss functions over continuous variables.

**Adaptability** is a feature of a system or of a process. Adaptability can be understood as the ability of a system to adapt itself efficiently and fast to changed circumstances. An adaptive system is therefore an open system that which is able to fit its behaviour according to changes in its environment or in parts of the system itself. That is why a requirement to recognize the demand for change without any other factors involved can be expressed.

**Importacnt Point**: *"Adaptability in the field of organizational management can in general be seen as an ability to change something or oneself to fit to occurring changes."*

*–Andresen and Gronau*

With respect to business and manufacturing systems and processes adaptability has come to be seen increasingly as an important factor for their efficiency and economic success. To determine the adaptability of a process or a system, it should be validated concerning some criteria.

## 3.10 CORPORATE CULTURE

Organizational culture is the combined behaviour of humans who are part of an organization and the meanings that the people attach to their actions. Culture includes the organization values, visions, norms, working language, systems, symbols, beliefs and habits. It is also the pattern of such collective behaviours and assumptions that are taught to new organizational members as a way of perceiving, and even thinking and feeling. Organizational culture affects the way people and groups interact with each other, with clients and with stakeholders.

### REVIEW QUESTIONS

1. List and describe management functions. (R.G.P.V., Dec. 2010)
2. What is management? List theories of management and explain anyone. (R.G.P.V., Dec. 2009)
3. What is scope of management? Show and explain the functional areas of management.

4. Explain the different functions of management. Discuss the relative importance of the functions of management.
5. What are the schools of theories: (R.G.P.V., Dec. 2011
   (a) Classical School of Management(Administrative Management)
   (b) Bureaucratic Management
   (c) Classical School of Management.
6. What is knowledge driven learning organization?
7. Explain the concept of Hawthorne Experiments?
8. What is E-Business? Explain the advantage and disadvantage of E-Business.
9. What are the benefits of E-Commerce? Explain the application of E-Commerce.
10. What do you meant by corporate culture?

# 4 Organization Planning Departmentalization and Typology

## Chapter Outline



## 4.1 INTRODUCTION

The term organization is used in four different senses: as a process, as a structure of relationship, as a group of persons and as a system, as given below in Fig. 4.1:

(i) **Organization as a process:** Organization is dynamic process of managerial activity which is essential for planning the optimum utilization of company's resources for the various objectives.

(ii) **Organization as a framework of relationship:** Organization refers to the structure of relationships and among position jobs which is created to release certain objectives. Organization is the form of every human association for the attainment of a common purpose.

(iii) **Organization as a group of persons:** Organization is a group of persons contributing their efforts towards certain goals.

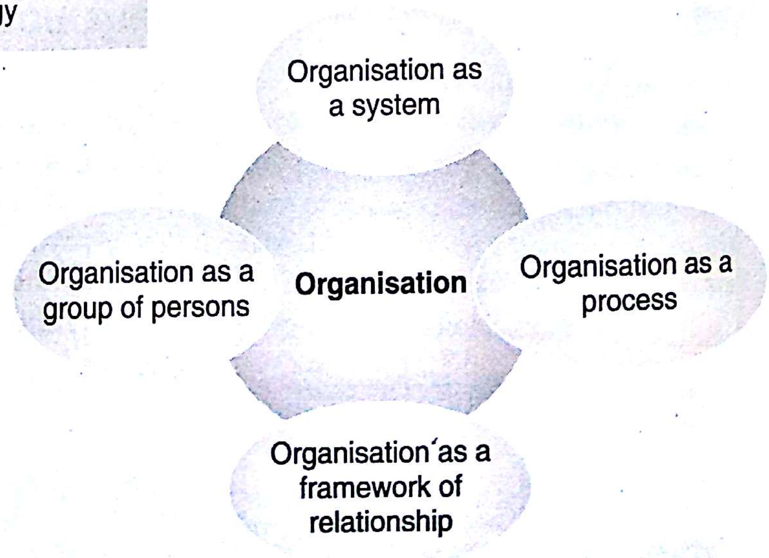


**Fig. 4.1 Organization**

**(iv) Organization as a system:** Organization is viewed as system or an arrangement.

### 4.1.1 Definition and Meaning of Organization

Different authors have defined organization in different ways. The main definitions of organization are as follows:

> **Important Point:** *"A goal oriented open system composed of people, structure and technology."*
>
> *Agrawal*
>
> *"A consciously coordinated social unit composed of two or more people that functions as a relatively continuous basis to achieve common goals or set of goals."*
>
> *Robbins*
>
> *"Organization is the process of identifying and grouping the work to be performed, defining and delegating responsibility and authority, and establishing relationship for the purpose of enabling people to work most effectively together in accomplishing objectives."*
>
> *Louis A. Allen*
>
> *"Organization may be defined as a group of individuals, large or small, that is cooperating under the direction of executive leadership in accomplishment of certain common object."*
>
> *Keith Davis*

From the above definitions, an organization has the following characteristics:

1. It is an open system.
2. It is a goal oriented.
3. It is a collection of people.
4. Organization consists of people.
5. Organization consists of technology.
6. It has continuity.

### 4.1.2 Features of Organization

The main characteristics or features of organization are as follows as shown in Fig. 4.2:

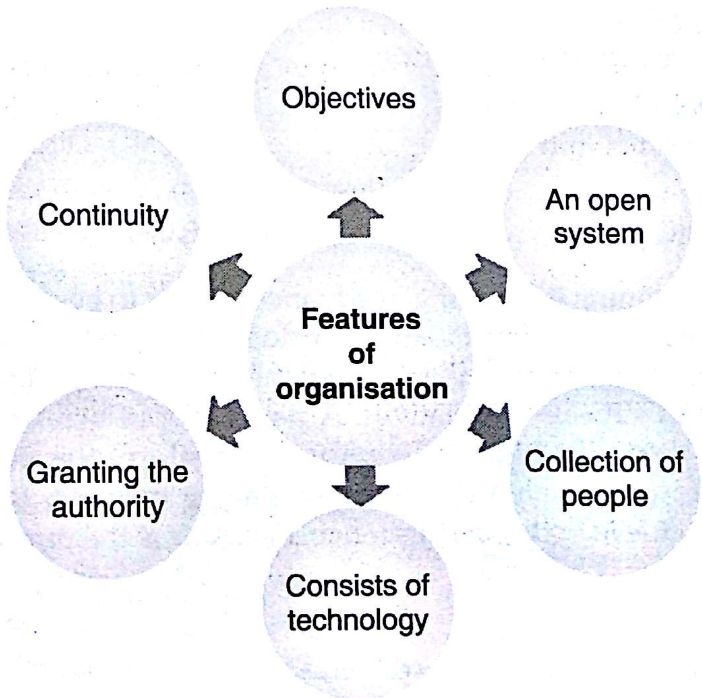


**Fig. 4.2** Features of Organization

1. **Objectives:** Born with the enterprise are its long-life objectives of profitable manufacturing and selling its products. Other objectives must be established by the administration from time to time to aid and support this main objective.
2. **An Open System:** An open system means open to environment. Organization exists and functions in environment. Environment compels the organization to acquire right type of people, technology and structure so that the goals to serve the environment can be attained. The organization is thus greatly influence by the environment.
3. **Collection of People:** People are the main performers in any organization. In other words, all the elements of any organization are the same except the people. Even with the same age, qualification, experience and facilities, the output of the people may vary.
4. **Consists of Technology:** Technology is the means of doing works. There are various ways of doing work. Technology originates a certain policy necessary to keep organizational beliefs in doings of the various people at different structural level. This saves the integrity of the people in achieving goals.
5. **Defining and Granting the Authority:** The authority and responsibility should be well defined and should correspond to each other. A close relationship between authority and responsibility should be established.
6. **Continuity:** As the organization involves people, and the people generate different needs, they can leave the organization or some may die too. This does not affect the organization to stop or lessen in size.

## 4.2 NATURE AND PURPOSE OF ORGANIZATION

Most socialist would agree that as human is part of an organization structure, they too need to find a way to integrate within the compound of organization. The nature of organization is to function as a whole and not as a system. Within the nature of organization, there exists workers and system that guides the organization. Nature of organizations is:

1. Maximizing profit.
2. Creating successful human culture.
3. Requiring optimum resources.
4. Creating perfect culture.

## 4.3 PLANNING

In simple words, planning is deciding in advance what is to be done, when where, how and by whom it is to be done. Planning bridges the gap from where we are to where we want to go. It includes the selection of objectives, policies, procedures and programs from various alternatives. A plan is a pre-determined course of action to achieve a specified goal. It is an intellectual process characterized by thinking before doing. It is an attempt on the part of manager to anticipate the future in order to achieve better performance. Planning is the primary function of management.

### 4.3.1 Meaning and Definition of Planning

Different authors have given different definitions of planning from time to time. The main definitions of planning are as follows:

> **Important Point:** *"Planning is deciding in advance what to do, how to do it, when to do it, and who is to do it. Planning bridges the gap from where we are to where we want to go. It makes it possible for things to occur which would not otherwise happen."* - Koontz & O'Donnel
>
> *Planning is a function that determines in advance what should be done. It consists of selecting the enterprise objectives, policies, programs, procedures and other means of achieving these objectives. In planning, the manager must decide which of the alternative plans are to be followed and executed. Planning is intellectual in nature. It is a mental work. It is thinking ahead and preparing for the future.* - Theo Haimann
>
> *"A plan is a trap laid to capture the future."* -According to Allen

### 4.3.2 Characteristics of Planning

1. **Planning is goal-oriented:** Goal orientation describes the actions of people and organizations regarding their primary aims. In business, goal orientation is a type of strategy that affects how the company approaches its revenues and plans for future projects. While all businesses are naturally goal oriented in some way, goal orientation plays an important role in focus and fund allocation. Goal orientation also plays a part in management styles and information technology projects.
   - Planning is made to achieve desired objective of business.
   - The goals established should general acceptance otherwise individual efforts and energy may go misguided and misdirected.
   - Planning identifies the action that would lead to desired goals quickly and economically.
   - It provides sense of direction to various activities. E.g. Maruti Udhyog is trying to capture once again Indian Car Market by launching diesel models.
2. **Planning is looking ahead:** Planning is looking ahead is true because it contributes heavily to success and gives us some control over the future. By planning we set aside our tasks and deadlines so that we can enlarge our mental focus and notice the bigger picture. By planning we can set organizational goals and for this certainly we have to look ahead.
   - Planning is done for future.
   - It requires peeping in future, analyzing it and predicting it.
   - Planning is based on forecasting.
   - A plan is a synthesis of forecast.
   - It is a mental pre-disposition for things to happen in future.
3. **Planning is an intellectual process:** Planning is an intellectual process of thinking in advance. It is a process of deciding the future on the series of events to follow. Planning is a process where a number of steps are to be taken to decide the future course of action. Managers or executives have to consider various courses of action, achieve the desired goals, go in details of

the pros and cons of every course of action and then finally decide what course of action may suit them best. Thus:

- Planning is a mental exercise involving creative thinking, sound judgement and imagination.
- It is not a mere guesswork but a rational thinking.
- A manager can prepare sound plans only if he has sound judgement, foresight and imagination.
- Planning is always based on goals, facts and considered estimates.

4. **Planning is the primary function of management/Primacy of Planning:** Planning lays foundation for other functions of management.
   - It serves as a guide for organizing, staffing, directing and controlling.
   - All the functions of management are performed within the framework of plans laid out.
   - Planning is the basic or fundamental function of management.
5. **Planning is a Continuous Process:** According to George R. Terry, "Planning is a continuous process and there is no end to it. It involves continuous collection, evaluation and selection of data, and scientific investigation and analysis of the possible alternative courses of action and the selection of the best alternative.
   - Planning is an eternal function due to the dynamic business environment.
   - Plans are also prepared for specific period of time and at the end of that period, plans are subjected to revaluation and review in the light of new requirements and changing conditions.
   - Planning never comes into end till the enterprise exists issues, problems may keep cropping up and they have to be tackled by effective planning.
6. **Planning is designed for efficiency:** Planning leads to accomplishment of objectives at the minimum possible cost.
   - It avoids wastage of resources and ensures adequate and optimum utilization of resources.
   - A plan is worthless or useless if it does not value the cost incurred on it.
   - Planning must lead to saving of time, effort and money.
   - Planning leads to proper utilization of men, money, materials, methods and machines.

## 4.4 LEVELS OF PLANNING

A plan is a pre-determined course of action to achieve a specified goal. It is an intellectual process characterized by thinking before doing. Planning function of management involves following steps as shown in Fig. 4.3.

1. **Establishment of objectives:** Planning starts with the setting of goals and objectives to be achieved. Objectives provide a rationale for undertaking various activities as well as indicate direction of efforts.
2. **Establishment of Planning Premises:** Planning premises are the assumptions about the lively shape of events in future. They serve as a basis of planning.

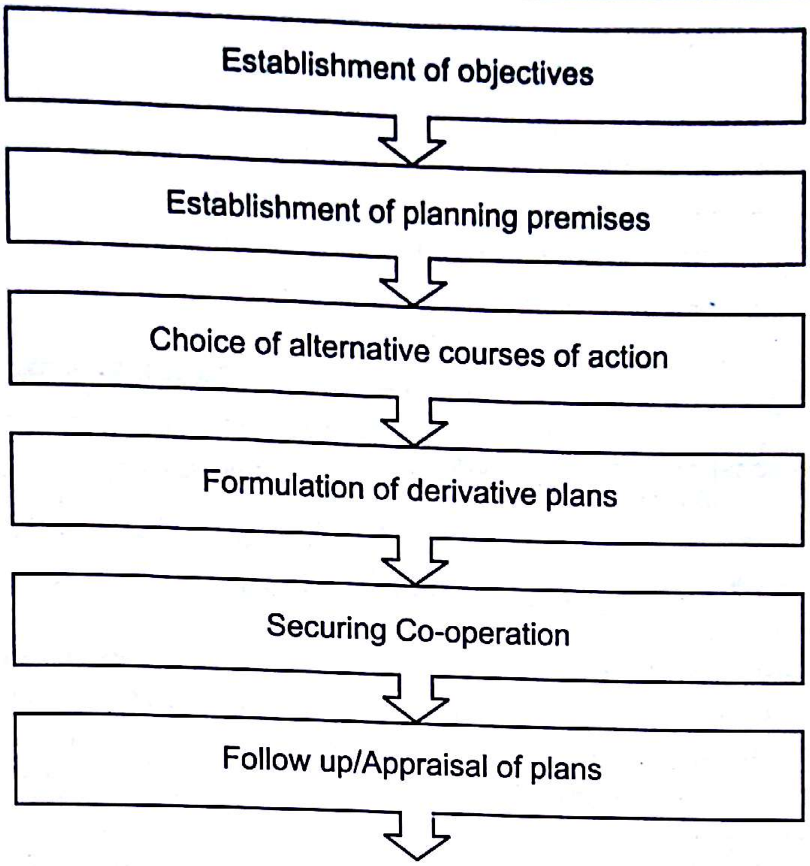


Fig. 4.3 Levels of Planning

3. **Choice of alternative courses of action:** When forecasting is available and premises are established, a number of alternative courses of action have to be considered. For this purpose, each and every alternative will be evaluated by weighing its pros and cons in the light of resources available and requirements of the organization.
4. **Formulation of derivative plans:** Derivative plans are the sub-plans or secondary plans which help in the achievement of main plan. Secondary plans flows from the basic plan. These are meant to support and expedite the achievement of basic plans.
5. **Securing Co-operation:** After the plans have been determined, it is necessary rather advisable to take subordinates or those who have to implement these plans into confidence.
6. **Follow up/Appraisal of plans:** After choosing a particular course of action, it is put into action. This step establishes a link between planning and controlling function.

## 4.5 DIFFICULTIES IN PLANNING

There are several difficulties of planning. Some of them are inherent in the process of planning like rigidity and other arise due to shortcoming of the techniques of planning and in the planners themselves. The difficulties in planning are as shown in Fig. 4.4.

**Important Point:** *"Expenses on planning should never exceed the estimated benefits from planning."* *-Koontz and O'Donell,*

1. **Make administration Inflexible:** Planning has tendency to make administration inflexible. Planning implies prior determination of policies, procedures and programs and a strict adherence to them in all circumstances. There is no scope for individual freedom.

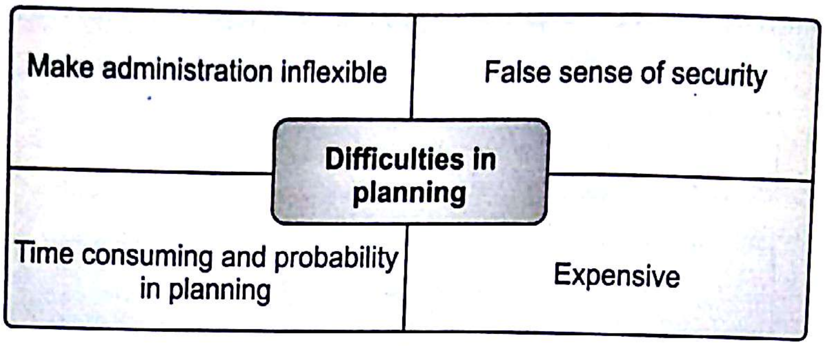


Fig. 4.4 Difficulties in Planning

2. **Time consuming:** Planning is not suitable during emergency or crisis when quick decisions are required. It is because planning is a time consuming process as it involves collection of information, its analysis and interpretation thereof. This entire process takes a lot of time specially where there are a number of alternatives available.
3. **Probability in planning:** Planning is based on forecasts which are mere estimates about future. These estimates may prove to be inexact due to the uncertainty of future. Any change in the anticipated situation may render plans ineffective.
4. **False sense of security:** Elaborate planning may create a false sense of security to the effect that everything is taken for granted. Managers assume that as long as they work as per plans, it is satisfactory. Therefore, they fail to take up timely actions and an opportunity is lost.
5. **Expensive:** Collection, analysis and evaluation of different information, facts and alternatives involves a lot of expense in terms of time, effort and money.

## 4.6 MANAGEMENT BY OBJECTIVE (MBO)

Management by objective (MBO) is the most widely accepted philosophy of management today which is a demanding and rewarding style of management.

> **Important Point:** *"MBO is a process whereby superior and subordinate managers of an organization jointly define its common goals define each individual's major areas of responsibility in terms of results expected of him and use these measures as guides for operating the unit and assessing the contribution of each of its members."*
>
> *-George Odiome*
>
> *"MBO is a dynamic system which seeks to integrate the company's needs to clarify and achieve its profits and growth goals with the manager's need to contribute and develop himself. It is a demanding and rewarding style of managing a business."*
>
> *-John Humble*

**Peter Drucker** outlined the five-step process for MBO as shown in Fig. 4.5. Each stage has particular challenges that need to be addressed for the whole system to work effectively.

These steps are explained below:

1. **Set organizational objectives:** MBO starts with clearly defined strategic organizational objectives. If the organization is not clear where it is going, no one working there will be able to achieve the goal.
2. **Cascading objectives down to employees:** To support the mission, the organization needs to set clear goals and objectives, which then need to cascade down from one organizational level to the next until they reach to everyone to make MBO goals and objectives setting more effective. Drucker used the 'SMART' acronym to set goals that were attainable and to which people felt accountable. He said that goals and objectives must be:

   S → Specific
   M → Measurable
   A → Agreed (relating to the participative management principle)
   R → Realistic
   T → Time related

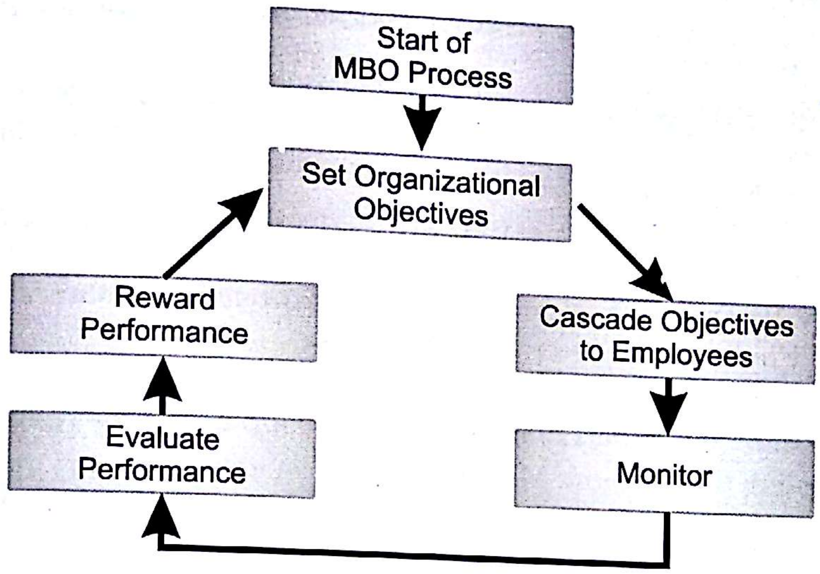


**Fig. 4.5** Five-step process for MBO

3. **Encourage participation in goal setting:** Everyone needs to understand how their personal goals fit with the objectives of the organization. This is best done when goals and objectives at each level are shared and discussed, so that everyone understands "why" things are being done, and then sets their own goals to align with these. This increases people's ownership of their objectives. Rather than blindly following orders, managers, supervisors, and employees in an MBO system know what needs to be done and thus need not be ordered around. By pushing decision-making and responsibility down through the organization, mangers motivate people to solve the problems they face and give them the information they need to adapt flexibly to changing circumstances.
4. **Monitor Progress:** Because the goals and objectives are SMART, they are measurable. They do not measure themselves though, so supervisor have to create a monitoring system that signals when things are off track. This monitoring system has to be timely enough so that issues can be dealt with

before they threaten goal achievement. With the cascade effect, no goal is set in isolation, so not meeting targets in one area will affect targets everywhere.

5. **Evaluate and reward performance:** MBO is designed to improve performance at all levels of the organization. To ensure this happens, superiors need to put a comprehensive evaluation system in place. As goals have been defined in a specific, measurable and time-based way, the evaluation aspect of MBO is relatively straight forward. Employees are evaluated on their performance with respect to goal achievement (allowing appropriately for changes in the environment.) All that is left to do is to tie goal achievement to reward, and perhaps compensation, and provide the appropriate feedback.

### 4.6.1 Advantages of MBO

Management by objective (MBO) has following advantages:

1. **MBO is a result-oriented philosophy:** It does not favor management by crisis. Managers are expected to develop specific individual and group goals, develop appropriate action plans, properly allocate resources and establish control standards.
2. **Goal-setting is typically an annual feature:** MBO produces goals that identify desired/expected results. Goals are made verifiable and measurable which encourage high level of performance.
3. **Decision-making:** It participative decision-making and two-way communication encourages the subordinate to communicate freely and honestly. Participation, clearer goals and improved communication will go a long way in improving morale of employees.
4. **Planning process:** MBO programs sharpen the planning process in an organization. It compels managers to think of planning by results.
5. **Accomplish the mission:** MBO gives an individual or group, opportunity to use imagination and creativity to accomplish the mission. Managers devote time for planning results.
6. **Develop personal leadership:** Continuous monitoring is an essential feature of MBO. This is useful for achieving better results. MBO helps individual manager to develop personal leadership and skills useful for efficient management of activities of a business unit.

### 4.6.2 Limitations of MBO

MBO have following disadvantages:

1. MBO is time-consuming process. Objectives, at all levels of the organization are set carefully after considering pros and cons which consumes lot of time.
2. MBO is pressure-oriented program. It is based on reward-punishment psychology. It tries to indiscriminately force improvement on all employees.
3. Considerable difficulties may be encountered while co-ordinating objectives of the organization with those of the individual and the department. Managers may face problems of measuring objectives when the objectives are not clear and realistic.
4. MBO can function successfully provided measurable objectives are jointly set and it is agreed upon by all. Problems arise when:

(a) Verifiable goals are difficult to set.

(b) Goals are inflexible and rigid.

(c) Goals tend to take precedence over the people who use it.

(d) Greater emphasis on quantifiable and easily measurable results instead of important.

5. Lack of appreciation of MBO is observed at different levels of the organization. This may be due to the failure of the top management to communicate the philosophy of MBO to entire staff and all departments.

## 4.7 BCG MATRIX

A chart of four celled matrix (2x2 matrixes) had been created by **Bruce Henderson** for the **Boston Consulting Group (BCG)**, USA in 1968 to help corporations with analyzing their business units or product lines. It is the most renowned corporate portfolio analysis tool. It provides a graphic representation for an organization to examine different businesses in its portfolio on the basis of their related market share and industry growth rates. It is a two dimensional analysis on management of Strategic Business Units (SBU's). In other words, it is a comparative analysis of business potential and the evaluation of environment.

The BCG Matrix can be used during value chain selection as a tool to quickly assess the market share of the local value chain against the growth of the globalized market in which it competes. Often the necessary data can be collected easily from secondary sources. This tool though fairly low cost and easy to employ only gives a static snapshot of the value chain's performance in an market and is not capable of describing the market dynamics or the potential for change. We had that simple BCG matrix-which looked at the business growth rate and one's relative position in the market.

BCG matrix has four cells, with the horizontal axis representing relative market share and the vertical axis denoting market growth rate. The mid-point of relative market share is set at 1.0, if all the SBU's are in same industry, the average growth rate of the industry is used. While, if all the SBU's are located in different industries, then the mid-point is set at the growth rate for the economy.

Resources are allocated to the business units according to their situation on the grid. The four cells of this matrix have been called as **Stars, Cash Cows, Question Marks and Dogs**. Each of these cells represents a particular type of business. We had a simple and peaceful 2 x 2 matrix as shown in Fig. 4.6.

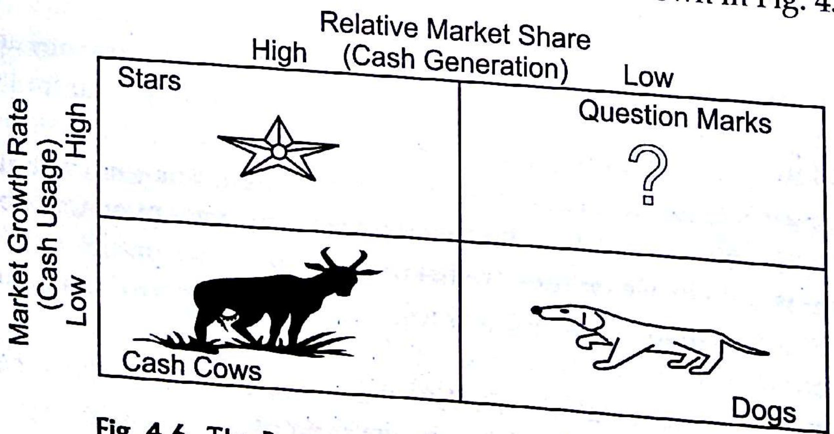


**Fig. 4.6** The Boston Consulting Group (BCG) Matrix

Each quadrant of the matrix describes the status of the value chain against its competitors and suggests its potential for competitiveness:

1. **Stars**: Stars represent business units having large market share in a fast growing industry. They may generate cash but because of fast growing market, stars require huge investments to maintain their lead. Net cash flow is usually modest. SBU's located in this cell are attractive as they are located in a robust industry and these business units are highly competitive in the industry. If successful, a star will become a cash cow when the industry matures.
2. **Cash Cows**: Cash cows represent business units having a large market share in a mature, slow growing industry. Cash cows require little investment and generate cash that can be utilized for investment in other business units. These SBU's are the corporation's key source of cash, and are specifically the core business. They are the base of an organization. These businesses usually follow stability strategies. When cash cows loose their appeal and move towards deterioration, then a retrenchment policy may be pursued.
3. **Question Marks**: Question marks represent business units having low relative market share and located in a high growth industry. They require huge amount of cash to maintain or gain market share. They require attention to determine if the venture can be viable. Question marks are generally new goods and services which have a good commercial prospective. There is no specific strategy which can be adopted. If the firm thinks it has dominant market share, then it can adopt expansion strategy, else retrenchment strategy can be adopted. Most businesses start as question marks as the company tries to enter a high growth market in which there is already a market-share. If ignored, then question marks may become dogs, while if huge investment is made, and then they have potential of becoming stars.
4. **Dogs**: Dogs represent businesses having weak market shares in low-growth markets. They neither generate cash nor require huge amount of cash. Due to low market share, these business units face cost disadvantages. Generally retrenchment strategies are adopted because these firms can gain market share only at the expense of competitor's/rival firms. These business firms have weak market share because of high costs, poor quality, ineffective marketing, etc. Unless a dog has some other strategic aim, it should be liquidated if there are fewer prospects for it to gain market share. Number of dogs should be avoided and minimized in an organization.

### 4.7.1 Limitations of BCG Matrix

The BCG Matrix produces a framework for allocating resources among different business units and makes it possible to compare many business units at a glance. But BCG Matrix is not free from limitations, such as-

1. BCG matrix classifies businesses as low and high, but generally businesses can be medium also. Thus, the true nature of business may not be reflected.
2. Market is not clearly defined in this model.
3. High market share does not always leads to high profits. There also high costs are involved with high market share.
4. Growth rate and relative market share are not the only indicators of profitability. This model ignores and overlooks other indicators of profitability.

5. At times, dogs may help other businesses in gaining competitive advantage. They can earn even more than cash cows sometimes.
6. This four-celled approach is considered as to be too simplistic.

## 4.8 GE –MCKINSEY MATRIX

GE- McKinsey matrix came with the same kind of axis (though with slightly different terminologies) but with a twist: now you had to navigate through a 3 x 3 matrix and 9 cells instead of 4 as shown in the Fig. 4.7.

1. The three cells at the top left hand side of the matrix are the most attractive in which to operate and require a policy of investment for growth – these are usually coloured green.

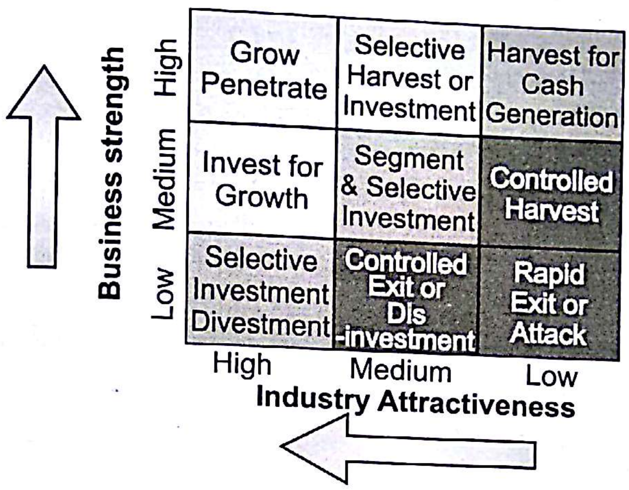


Fig. 4.7 GE –McKinsey Matrix

2. The three cells running diagonally from left to right have a medium attractiveness, are coloured yellow and the management of businesses within this category should be more cautious and with a greater emphasis being placed on selective investment and earning retention.
3. The three cells at the bottom right hand side are the least attractive, therefore coloured red and management should follow a policy of harvesting and/or divesting unless the relative strengths can be improved.

Channon and McCosh devised a set of generic investment strategies for the GE McKinsey matrix as labeled in the previous diagram. A. T. Kearney (ATK) also put forward guidelines for strategies in the different boxes and where these have not been incorporated they are mentioned below.

(a) **Grow/Penetrate:** These businesses are a target for investment, they have strong business strengths, are in attractive markets and they should therefore have high returns on investment and competitive advantage. They should receive financial and managerial support to maintain their strong position and to continue contributing to long-term profitability. Thus these businesses:
   - Seek dominance
   - Grow
   - Maximize investment

(b) **Invest for Growth:** Businesses here are in very attractive industries but have average business strength. They should be invested in to improve their long-term competitive position. Thus these businesses:

- Evaluate potential for leadership via segmentation
- Identify weaknesses
- Build strengths

(c) **Selective Investment or Divestment:** These businesses are in very attractive markets but their business strength is weak. Investment must be aimed at improving the business strengths. These businesses will probably have to be funded by other businesses in the group as they are not self-funding. Only businesses that can improve their strengths should be retained – if not they should be divested. These businesses should:

- Specialize
- Seek niches
- Consider acquisitions

(d) **Selective Harvest or Investment:** Businesses in this box have good business strength in an industry that is losing its attractiveness. They should be supported if necessary but they may be self-supporting in cash flow terms. Selective harvesting is an option to extract cash flow but this should be done with caution so as not to run down the business prematurely. Thus they should:

- Identify growth segments
- Invest strongly
- Maintain position elsewhere

(e) **Segment and Selective Investment:** Businesses with average business strengths and in average industries can improve their positions by creative segmentation to create profitable segments and by selective investment to support the segmentation strategy. The business needs to create superior returns by concentrating on building segment barriers to differentiate themselves. The guidelines for such businesses are:

- Identify growth segments
- Specialize
- Invest selectively

(f) **Controlled Exit or Harvest:** Businesses with weak business strengths in moderately attractive industries are candidates for a controlled exit or divestment. Attempts to gain market share by increasing business strengths could prove to be very expensive and must be done with caution. Thus the following guidelines should be followed:

- Specialize
- Seek niches
- Consider exit

(g) **Harvest for Cash Generation:** Strong businesses in unattractive markets should be net cash generators and could provide funds for use throughout the rest of the portfolio. Investment should be aimed at keeping these businesses in a dominant position of strength but over

investment can be disastrous especially in a mature market. Be aware of competitors trying to revitalize mature industries. In this case the following guidelines would be useful:

- Maintain overall position
- Seek cash flow
- Invest at maintenance level

(h) **Controlled Harvest:** They have average business strengths in an unattractive market and the strategy should be to harvest the business in a controlled way to prevent a defeat or the business could be used to upset a competitor. The guidelines are:

- Prune (Reduce) lines
- Minimize investment
- Position to divest

(i) **Rapid Exit or Attack Business:** These businesses have neither strengths nor an attractive industry and should be exited. Investments made should only be done to fund the exit.

- Trust leaders statesmanship
- Go after competitors cash generators
- Time exit and divest

## 4.9 SWOT ANALYSIS

A company when revenue, cost and expense targets are not being achieved its market share is dropping and industry conditions are unfavourable. If entrepreneur wants to launch a new business venture; etc then the company needs SWOT analysis.

**Important Point:** *SWOT is a technique that enables a group or individual to move from everyday problems and traditional strategies to a fresh perspective.*

The objective of SWOT analysis is to take the advantage of strengths and opportunities of company. It minimizes weaknesses and eliminates threats.

SWOT is a contraction for:

**S–Strengths, W–Weaknesses, O–Opportunities, T – Threats.**

SWOT is a strategic planning method used to evaluate- internal environment and external environment as shown in Fig. 4.8.

| | |
|---|---|
| **S**–Strengths<br>**W**–Weaknesses | } Internal Environment |
| **O**–Opportunities<br>**T**–Threats | } External Environment |

**Fig. 4.8 SWOT**

1. **Strength:** They are any existing or potential resources or capability within the organization that provides a competitive advantage in the market. Example: Strong distribution network intense staff commitment and loyalty increasing profit margin.
2. **Weakness:** They are any existing or potential force which could serve as a barrier to maintaining or achieving a competitive advantage in the market. Example: Lack of a clear company strategy, lack of training opportunities for using new software.
3. **Opportunity:** These are any existing or potential force in the external environment that, if properly leveraged, could provide a competitive advantage.

   Example: Organization's geographic location and new technology.
4. **Threats:** These are existing or potential force in the external environment that could erode a competitive advantage.

   Example: A new competitor entrant, a recession, rising interest rates, or tight credit lines.

## 4.10 STEPS IN DECISION MAKING

Decision making is a daily activity for any human being. There is no exception about that. When it comes to business organizations, decision making is a habit and a process as well. Effective and successful decisions make profit to the company and unsuccessful ones make losses. Therefore, corporate decision making is the most critical process in any organization. Decision making is at the heart of organizational effectiveness, climate, and health.

**Important Point:** *Decision making is process of examining possibilities, options, comparing them, and choosing a best course of action.*

There are two dominant issues affect how decisions are made in organizations.

(i) **Stability:** It is application of existing practices and maintenance of existing performance levels.

(ii) **Change:** It is environmental demands for quick response and emerging problems that are ambiguous.

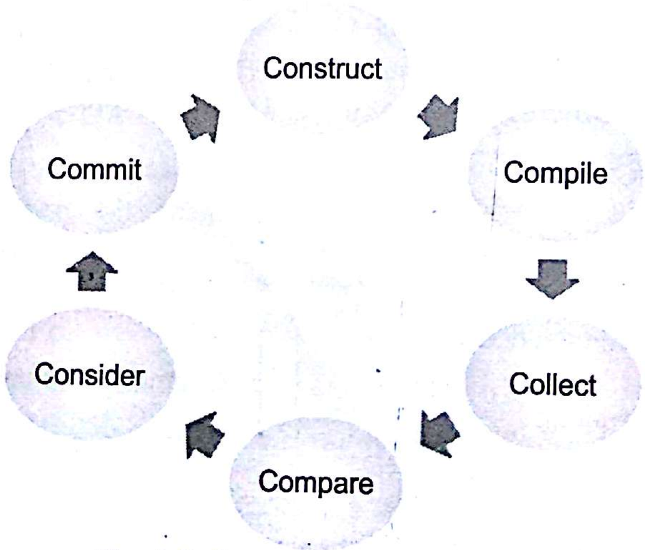


**Fig. 4.9 Six C's of Decision Making**

A participative decision making structures are required to effectively manage change. There are 6C's of decision making as shown in Fig. 4.9.

1. **Construct.** It is the clear picture of precisely what must be decided.
2. **Compile.** It is a list of requirements that must be met.
3. **Collect.** It is information on alternatives that meet the requirements.
4. **Compare.** Describe the alternatives that meet the requirements.
5. **Consider.** Represent what might go wrong and the factor with each alternative.
6. **Commit** to a decision and follow through with it.

Six steps in the decision making process are shown in Fig. 4.10 discussed below.

1. **Identifying the problem**: In this step, the problem is thoroughly analyzed. There are a couple of questions one should ask when it comes to identifying the purpose of the decision.
   - What exactly is the problem?
   - Why the problem should be solved?
   - Who are the affected parties of the problem?
   - Does the problem have a deadline or a specific time-line?
2. **Developing alternative solutions**: After defining and analyzing the real problem, the manager should develop (make) alternate (different) solutions for solving the problem. Only realistic solutions should be considered. Group participation and computers should be used for developing alternative solutions.
3. **Analyzing the alternative**: It carefully evaluates the merits and demerits of each alternative solution. He should compare the cost of each solution and the risks involved. He should also compare the feasibility of each solution that gives the best. He should find out which solution will be accepted by the employees.

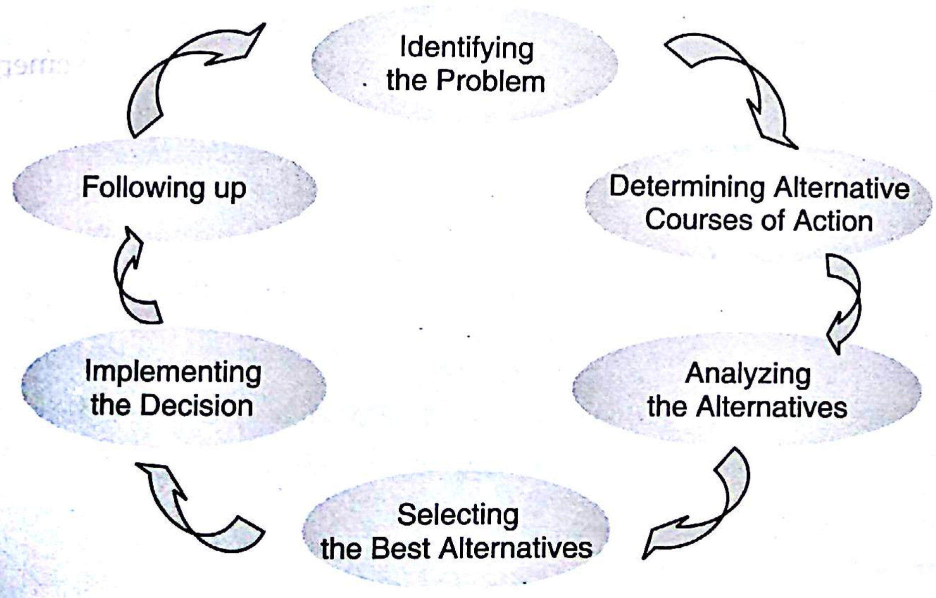


**Fig. 4.10 Six steps in the decision making process**

4. **Selecting the best alternatives:** In this process the manager should select a solution which has the most merits and least demerits. The best solution is called the "Decision".
5. **Implementing the Decision:** After making the decision, the manager should implement it. It required providing the employees with all the resources, which are required for implementing the decision. He should also motivate them to implement the decision.
6. **Follow Up:** After implementing the decision, the manager must do follow up. That is, he must get the feedback about the decision.

## 4.11 PRINCIPLES OF ORGANIZATION

There is no unanimity as to number of principles of organization amongst the leading authors on the subject. The main principles of organization are as shown in Fig. 4.11:

1. **Principle of Objective:** Every enterprise, big or small, prescribes certain basic objectives. Organization serves as a tool in attaining these prescribed objectives. Every part of the organization and the organization as a whole should be geared to the basic objective determined by the enterprise.

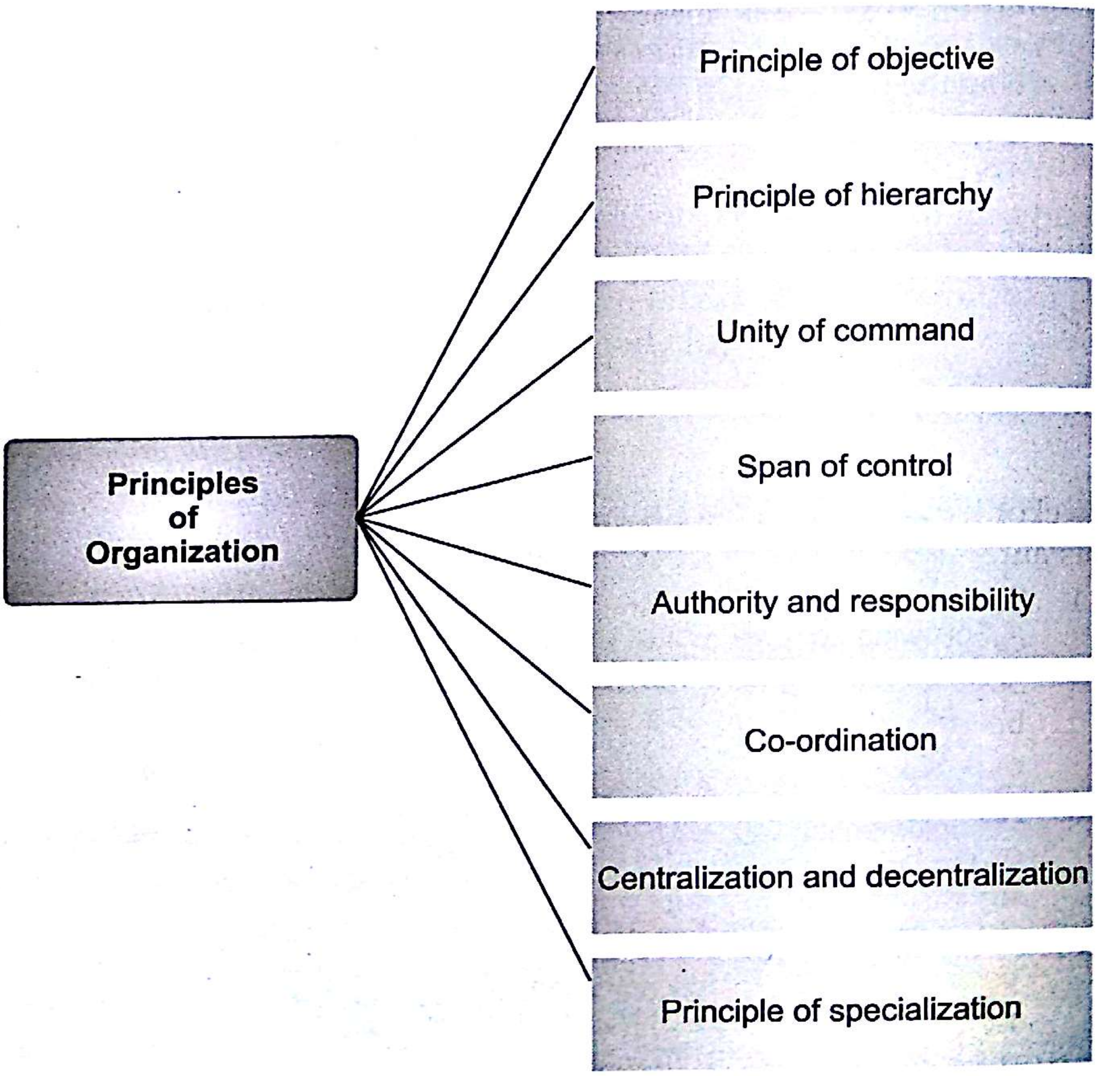


**Fig. 4.11** Principle of Organization

2. **Principles of Hierarchy:** It means control of higher over the lower – pyramidical organization wherein 'scalar chain' means the grading of duties according to degree of authority.

**Important Point:** *"Every organization must have a scalar chain just as every house must have its drain."* *–Urwick*

3. **Unity of Command:** Employee should receive orders from superior (only single boss mono-command) as normally followed in military.

**Important Point:** *"Employee should receive orders from one superior only." Fayol*

The example of unity of command principle is shown in Fig. 4.12. The principle has two faces:

(i) A single determinate person to issue order.

(ii) The order should not be conflicting to confuse them.

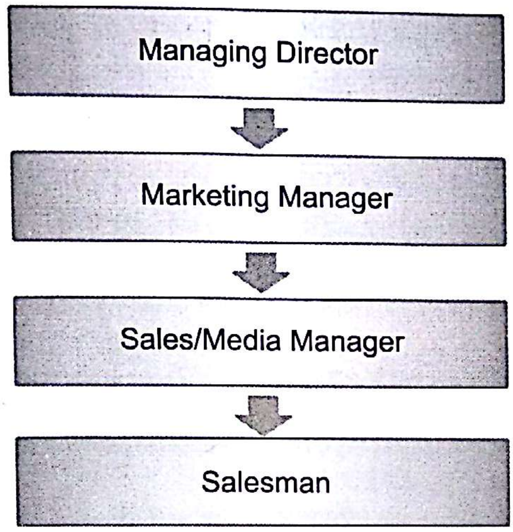


**Fig. 4.12** Unity of command

According to the above diagram, the Managing Director has got the highest level of authority. This authority is shared by the Marketing Manager who shares his authority with the Sales Manager.

4. **Span of Control:** Number of subordinates or the units of work that an officer can personally direct, control and supervise also known as "Span of Supervision" or Span of Management or Span of Control. Span is the length between the thumb and the little finger. Symbolically, it refers to one's hold over something.
5. **Authority and Responsibility:** Authority signifies hold over knowledge, skill or position. The role of authority is like soul to the body. Administrators do not actually perform duty directly but they get things done. The right to get things done is called authority. Authority is legal or rightful power, a right to command or to act. In formal organization it is vested with job position and not to the person. Hence it is a bureaucratic concept. Organizations where authority and responsibility are clearly defined are good and less corrupt and hence termed as: Two Pillars on which organization is sustained.

**Important Point:** *"It is right to give orders and power to exact obedience."* Fayol

6. **Co-ordination:** It is the process of bringing about unity and harmony of functioning among the diverse elements and sub systems of an organization.

**Important Point:** *"Executive develops an orderly pattern and secures unity of action."* McFarland

7. **Centralization and Decentralization:** These concepts are used to denote the Administrative or Management authority within an organization. Centralization is concentration of authority in one place while the decentralization is greater dispersion of authority. Centralization incline towards power and domination; the other inclines towards competition and self-determination. Centralization is also overload apex of the pyramid;

**Important Point:** *"Transfer of authority from lower to higher level is Centralization."* White

*"Decentralization of authority is a fundamental phase of delegation."* Koontz and O'Donnel

*"Every thing that goes to increase the importance of the subordinate's role is decentralization"* Koontz and O'Donnel

8. **Principle of Specialization:** According to the principle, the whole work of a concern should be divided amongst the subordinates on the basis of qualifications, abilities and skills. It is through division of work specialization can be achieved which results in effective organization.

## 4.12 TYPES OF ORGANIZATION

There are two types of organizations that are basically classified on the basis of relationships as shown in Fig. 4.13.

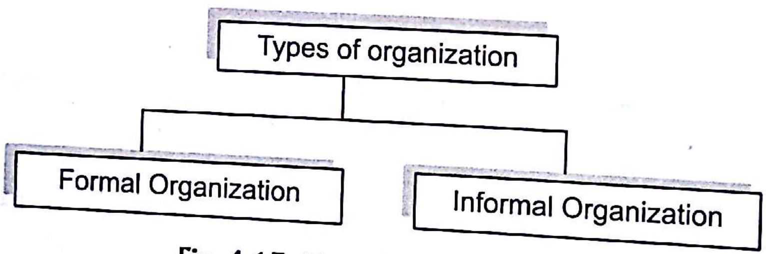


Fig. 4.13 Types of Organization

1. **Formal Organization:** This is one which refers to a structure of well defined jobs each bearing a measure of authority and responsibility. It is a conscious determination by which people accomplish goals by adhering to the norms laid down by the structure. This kind of organization is an arbitrary set up in which each person is responsible for his performance. Formal organization has a formal set up to achieve pre- determined goals.
2. **Informal Organization:** It refers to a network of personal and social relationships which spontaneously originates within the formal set up. Informal organizations develop relationships which are built on likes, dislikes, feelings and emotions. Therefore, the network of social groups based on

friendships can be called as informal organizations. There is no conscious effort made to have informal organization. It emerges from the formal organization and it is not based on any rules and regulations as in case of formal organization.

## 4.13 DIMENSIONS OF ORGANIZATIONS

The basic design dimensions are broad, and include the following:

1. **Behaviour formalization:** This is the degree to which the organization has official rules, regulations, and procedures. An organization may have a formal structure, but may operate informally.
2. **Size/specialization:** The larger the organization, the more likely the basic design dimension will be formalized, central, specialized, standardized, and complex. Additionally, the hierarchy of authority is typically a tall structure. Large organizations also reap the efficiency advantages of economies of scale. Specialization is the degree to which jobs are narrowly defined and depend on unique expertise.
3. **Authority centralization:** It describes the degree to which decisions are made at the top of the organization. The quality movement and programs that stress delegating responsibility and decision making to lower levels result in decentralization. At the same time, reductions in organizations have altered the middle management tier of the organization by eliminating part of the central reporting structure. Typically, the larger and longer the organization has been in existence, the more centralized will be its structure.

Richard Daft in his book "Organizational Theory and Design" organizes these dimensions into categories of structural and contextual.

(i) **Structural dimensions.** These include:

- **Centralization:** The extent to which functions are dispersed in the organization, either in terms of integration with other functions or geographically.
- **Formalization:** Regarding the extent of policies and procedures in the organization
- **Hierarchy:** Regarding the extent and configuration of levels in the structure.
- **Routinization:** Regarding the extent that organizational processes are standardized.
- **Specialization:** Regarding the extent to which activities are refined.
- **Training:** Regarding the extent of activities to equip organization members with knowledge and skills to carry out their roles.

(ii) **Contextual Dimensions.** They include:

- **Culture:** The values and beliefs shared by all (note that culture is often discerned by examining norms or observable behaviours in the workplace).
- **Environment:** The nature of external influences and activities in the political, technical, social and economic arenas.
- **Goals:** Unique overall priorities and desired end-states of the organization.

- **Size:** Number of people and resources and their span in the organization.
- **Technology:** The often unique activities required to reach organizational goals, including nature of activities, specialization, type of equipment/ facilities needed, etc.

## 4.14 DEPARTMENTALIZATION

Departmentalization is the process of grouping individual jobs in department. It involves grouping of activities and employees into departments so as to facilitate the accomplishment of organization objectives.

In another words, departmentalization refers to the process of grouping activities into departments. Division of labour creates specialists who need co-ordination. Thus coordination is facilitated by grouping specialists together in departments.

### 4.14.1 Need and importance of department

1. Specialization
2. Expansion
3. Autonomy
4. Fixation of responsibility
5. Appraisal
6. Management development
7. Administrative control

### 4.14.2 Types of Departmentalization

The following Fig. 4.14 shows the basic of departmentalization.

1. **Departmentalization by functional basis:** It is the grouping of activities in accordance with the function of an enterprise. Each major function of the enterprise is grouped into a department for example- human resources, IT, marketing, accounting, manufacturing, logistics, and engineering. Functional departmentalization can be used in all types of organizations.

   ***Merits:***

   1. It follows the principles of specialization.
   2. It is a logical and time proven method.
   3. Authority and responsibility can be clearly defined and fixed.
   4. Control shall become effective since the top managers are responsible for the end results.

   ***Demerits:***

   1. This type of departmentalization shall develop a loyalty towards the functions and not towards the enterprise as whole.
   2. Co-ordination of different function shall become difficult.
   3. Only the departmental heads are held responsible for defective work.

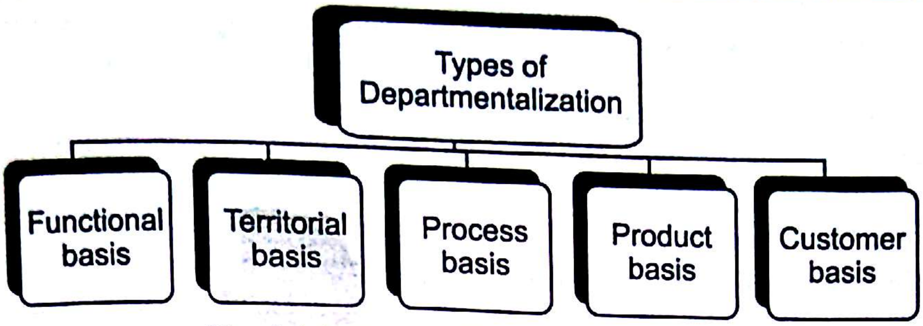


Fig. 4.14 Types of Departmentalization

2. **Departmentalization by territorial (geographical) basis:** A company may have separate departments to serve the southern region, northern region, etc. It has the advantage of the intimate knowledge of local conditions. For example, the organization structure of Coca-Cola has reflected the company's operation in two broad geographic areas – the North American sector and the international sector, which includes the Pacific Rim, the European Community, Northeast Europe, Africa and Latin America groups.

   ***Merits:***

   1. It motivates each regional head to achieve high performance.
   2. Provides each regional head an opportunity to adapt to his local situation and customer need with pace and accuracy.
   3. It affords valuable top-management training and experience to middle level executives enables the organization to take advantage of location factors, such as availability of raw materials, labour, market, etc.
   4. Enables the organization to compare regional performances and invest more resources in profitable regions and withdraw resources from unprofitable ones.

   ***Demerits:***

   1. It may give rise to duplication of various activities. Many routine and service functions performed by all the regional.
   2. Various regional units may become so engrossed in short run competition among them that they may forget the overall interest of the total organization.

3. **Departmentalization by process basis:** This is done on the basis of several discrete stages in the process or technologies involved in the manufacture of a product. A cotton textile mill has separate departments for ginning, spinning, weaving, dyeing and printing and packaging and sales.

   ***Merits:***

   1. It facilitates the use of heavy and costly equipment in an efficient manner.
   2. It follows the principle of specialization – each department is engaged in doing a special type of work. This increases efficiency.
   3. It is suitable for organizations which are engaged in the manufacturing those product which involve a number of processes.

   ***Demerits:***

   It is difficult to compare the performance of different process based departments.

4. **Departmentalization by product basis:** This is a grouping activity by product line. Tasks can also be grouped according to a specific product or service, thus placing all activities related to the product or the service under one manager. Each major product area in the corporation is under the authority of a senior manager who is specialist in, and is responsible for, everything related to the product line. LA gear is an example of company that uses product departmentalization. Its structure is based on its varied product lines which include women's footwear, children's footwear and men's footwear.

   ***Merits:***

   1. Relieves top management of operating task responsibility. It can therefore better concentrate on such centralized activities like finance, R& D and control.
   2. Enables the top management to compare the performance of different products and invest more resources in profitable products and withdraw resources from unprofitable ones.
   3. Those who work within a department derive greater satisfaction from identification with a recognizable goal.

   ***Demerits:***

   1. Results in duplication of staff and facilities
   2. Employment of large number of managerial personnel is required.

   Equipment in each product department may not be fully used.

5. **Departmentalization by Customer basis:** Any enterprise may be divided into a number of departments on the basis of the customers as shown in Fig. 4.15.

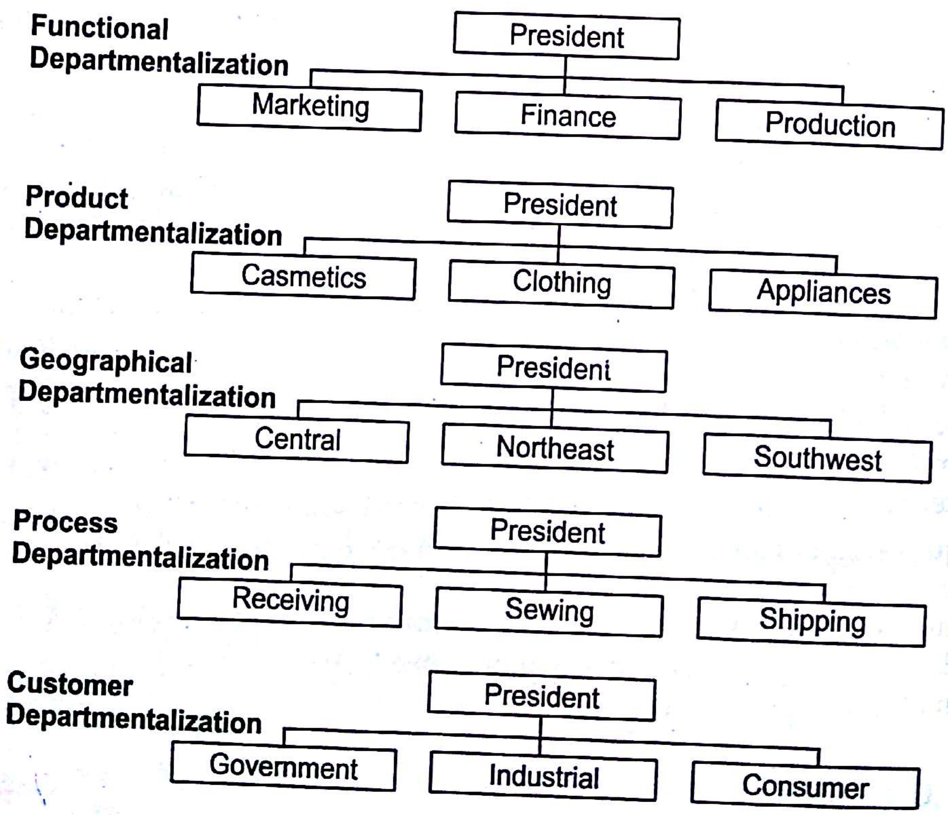


**Fig. 4.15** Departmentalization by Customer basis

For e.g., an educational institution may have separate departments for day, evening and distance learning course to impart education to full time students, locally employed students and outstation students respectively.

***Merits:***

It ensures full attention to major customer groups and helps the company to earn goodwill and create favourable image.

***Demerits:***

It may result in under utilization of resources and facilities in some department. There may be duplication of facilities.

## 4.15 SPAN AND LINE OF CONTROL

Number of subordinates or the units of work that an officer can personally direct, control and supervise also known as "Span of Supervision" or "Span of Management". It was termed as Span of Attention by Gracuinas. Span is the length between the thumb and the little finger. Symbolically it refers to one's hold over something. Following are the factors determining the span and line of control:

1. **Geographical dispersion**: If the branches of a business are widely dispersed, then the manager will find it difficult to supervise each of them, as such the span on control will be smaller.
2. **Capability of workers**: If workers are highly capable, need little supervision, and can be left on their own, e.g.: Theory Y type of people, they need not be supervised much as they are motivated and take initiative to work; as such the span of control will be wider.
3. **Capability of boss**: An experienced boss with good understanding of the tasks, good knowledge of the workers and good relationships with the workers, will be able to supervise more workers.
4. **Value added of the boss**: A boss that is adding value by training and developing new skills in the workers will need a narrow span of control than one who is focused only on performance management (this is the reverse of the capability of workers point above).
5. **Similarity of task**: If the tasks that the subordinates are performing are similar, then the span of control can be wider, as the manager can supervise them all at the same time.
6. **Volume of other tasks**: If the boss has other responsibilities, such as membership of committees, involvement in other projects, liaising with stakeholders, the number of direct reports will need to be smaller.
7. **Required administrative tasks**: If the boss is required to have regular face to face meetings, complete appraisal and development plans, discuss remuneration benefits, write job descriptions and employment contracts, explain employment policy changes and other administrative tasks then the span of control is reduced.

## 4.16 ORGANIZATION TYPOLOGY

Depending on the authority that is given to the person responsible for the project, the projects organization may take one of the following forms:

1. **Line Organization:** This is the oldest as well as the most common type of organization. It is also known as the military system as this type of organization is usually found in the army. The characteristic feature of this type is that, the line of authority flows vertically from the top executive to the lowest subordinate throughout the entire organizational structure. The authority is greatest at the top and reduces through each successive level down the organizational scale. A line organization with one level is shown in Fig. 4.16.

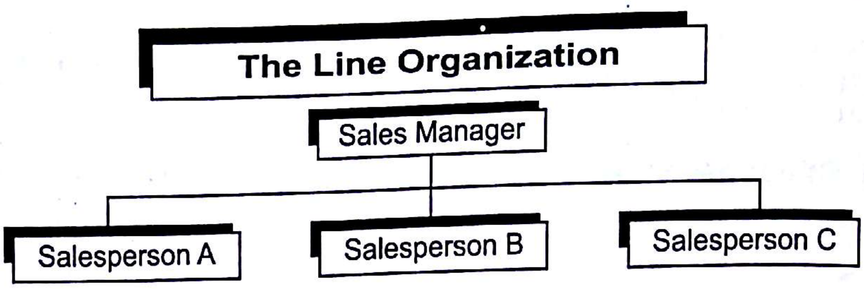


**Fig. 4.16** Line Organization with one Level

A variation of the pure line organization is the departmental line organization, under which the business enterprise is divided into several departments and the authority flows downward from the general manger through the departmental managers to the lower subordinates. The departmental heads are independent of each other and enjoy equal status. A two level line organization is shown in Fig. 4.17.

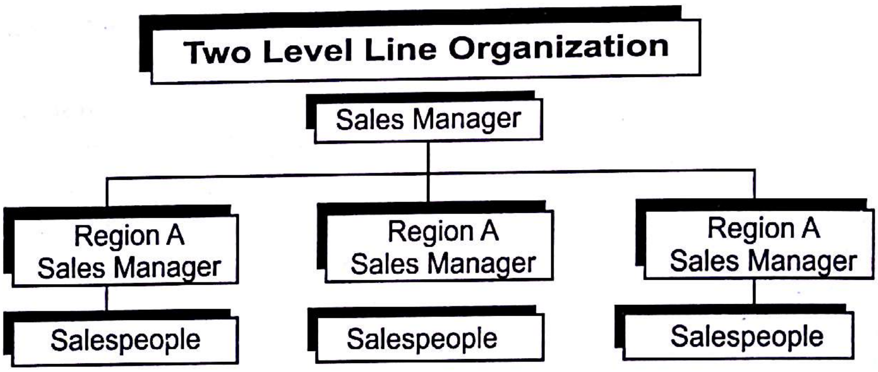


**Fig. 4.17** Line Organization with Two Levels

***Features:***

Line organization has the following characteristics:

(i) Lines of authority are vertical flowing from top to the bottom,

(ii) The command is through a straight and unbroken line. Each subordinate receives orders from one superior and is responsible to him alone.

(iii) All persons at the same level are independent of each other,

(iv) The authority and responsibility of each position is clearly defined and specified.

***Merits of Line Organization:***

1. It is the most simple and oldest method of administration.
2. In these organizations, superior-subordinate relationship is maintained and scalar chain of command flows from top to bottom.

3. The control is unified and concentrates on one person and therefore, he can independently make decisions of his own. Unified control ensures better discipline.
4. In this type of organization, every line executive has got fixed authority, power and fixed responsibility attached to every authority.
5. There is a co-ordination between the top most authority and bottom line authority. Since the authority relationships are clear, line officials are independent and can flexibly take the decision. This flexibility gives satisfaction of line·executives.

***Demerits of Line Organization:***

1. The line executive's decisions are implemented to the bottom. This results in over-relying on the line officials.
2. A line organization flows in a scalar chain from top to bottom and there is no scope for specialized functions. For example, expert advices whatever decisions are taken by line managers are implemented in the same way.
3. The policies and strategies which are framed by the top authority are carried out in the same way. This leaves no scope for communication from the other end. The complaints and suggestions of lower authority are not communicated back to the top authority. So, there is one way communication.
4. Whatever decisions are taken by the line officials, in certain situations wrong decisions, are carried down and implemented in the same way. Therefore, the degree of effective co-ordination is less.
5. The line officials have tendency to misuse their authority positions. This leads to autocratic leadership and monopoly in the concern.

2. **Line and Staff Organization:** Under this type, the organizational structure is basically that of the line organization, but "Staff, officers of functional experts are engaged to advise the line officers in the performance of their duties". Staff means something to lean on, and this is precisely the function of the staff officers. Line officers are the executives, and the staff officers are their advisers. The Fig. 4.18 shows the line and staff organization.

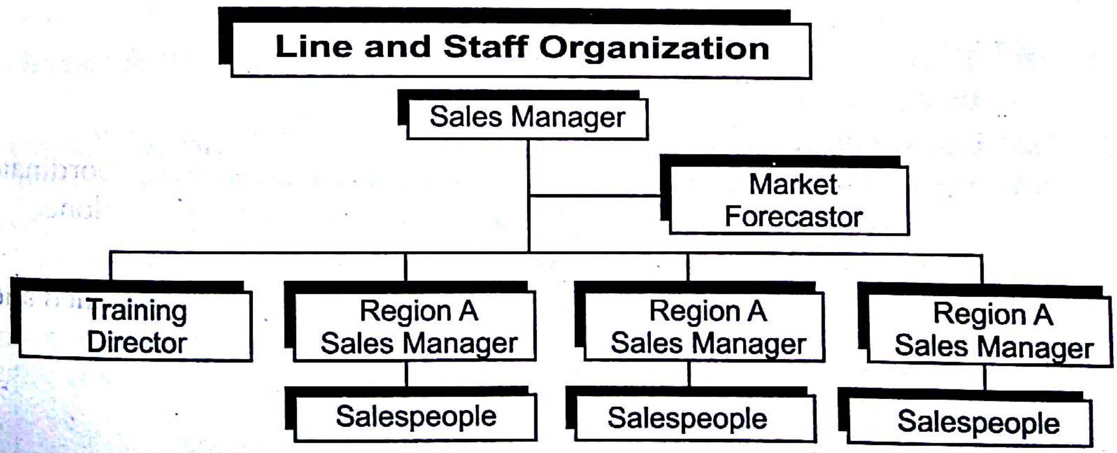


**Fig. 4.18** Line and staff Organization

***Merits of Line and Staff Organization:***

1. In a line and staff organization, the advice and counseling which is provided to the line executives divides the work between the two.
2. The line and staff organization facilitates expert advice to the line executive at the time of need.
3. Line and staff organization through specialization is able to provide better decision making and concentration remains in few hands. This feature helps in bringing co-ordination in work as every official is concentrating in their own area.
4. This gives a wide scope to the line executive to bring innovations and go for research work in those areas. This is possible due to the presence of staff specialists.
5. Due to the presence of staff specialists and their expert advice serves as ground for training to line officials. Line executives can give due concentration to their decision making. This in itself is a training ground for them.
6. Factor of specialization which is achieved by line staff helps in bringing co-ordination.

***Demerits of Line and Staff Organization:***

1. In a line and staff organization, there are two authorities flowing at one time. This results in the confusion between the two.
2. The workers are not able to understand as to who is their commanding authority.
3. The line official gets used to the expertise advice of the staff. At times the staff specialist also provides wrong decisions which the line executive has to consider. This can affect the efficient running of the enterprise.
4. Line and staff are two authorities, the factors of designations, status influence sentiments which are related to their relation, can pose a distress on the minds of the employees.
5. In line and staff concern, the concerns have to maintain the high remuneration of staff specialist. This proves to be costly for a concern with limited finance.
6. The power of concern is with the line official but the staff dislikes it as they are the one more in mental work.

3. **Functional Organization Structure:** Under functional organization the organization is divided into a number of functional areas. Each function is managed by functional expert in that area. Every functional area serves all other areas in the organization. For example, the purchase department handles purchases for all departments. Another example, the personnel manager will decide the questions relating to salary, promotions, transfers, etc., for every employee in the organization whether he is in production, sales or any other department.

***Features:***

The main characteristics of functional organization are as follows:

(i) The whole task of the enterprise is divided into specialized functions.

(ii) Each function is performed by a specialist.

(iii) The specialist in charge of a functional department has the authority over all other employees for his function.

(iv) Specialists operate with considerable independence.

***Advantages:***

1. Functional organization promotes logical division of work. Every functional head is an expert in his area and all workers get the benefit of his expertise.
2. Every functional head looks after one function only and, therefore, burden on top executives is reduced. Mental and manual functions are separated.
3. One man control is done away with and there is joint supervision of work. As a result, functional control becomes more effective.
4. Recruitment, selection and training of managers become simplified because each individual is required to have knowledge of one functional area only.
5. Every individual in the organization concentrates on one function only and receives the expert guidance from specialists.

***Disadvantages:***

1. A person is accountable to several superiors. As a result, his responsibility and loyalty get divided. In the absence of unity of command, responsibility for results cannot easily be fixed.
2. There are many cross relationships which create confusion. A worker may receive conflicting orders. He cannot easily understand his place in the organization. Discipline may be poor.
3. A decision problem requires the involvement of several specialists. Therefore, decision-making process in functional organization is slow.
4. Executives at lower level do not get opportunity of all-round experience. This may create problem in succession to top executive positions.

4. **Matrix Organization:** Matrix organization was introduced in USA in the early 1960's. Matrix organization is a combination of two or more organization structures. For example, functional organization and project organization. The organization is also divided on the basis of projects *e.g.*, Project X, Project Y, etc. Each project has a Project Manager *e.g.*, Project X Manager, Project Y Manager, etc. as shown in Fig. 4.19.

| Functional Manager / Project | Functional Manager A | Functional Manager B | Functional Manager C |
|---|---|---|---|
| Project Manager X | $A_1$ | $B_1$ | $C_1$ |
| Project Manager Y | $A_2$ | $B_2$ | $C_2$ |
| Project Manager Z | $A_3$ | $B_3$ | $C_3$ |

**Fig. 4.19 Matrix Organization: Flow of Project Authority**

A matrix, as shown in Fig 4.19, is a concept borrowed from algebra where an individual will abide by the decisions made by two superiors – one belonging to the project and the other to the specialized function. One will be like his direct boss and the other his project boss. Both are responsible for the successful completion of the project and therefore, both ought to have authority over the working force through whom the project is being executed. The following Fig. 4.19 shows the matrix organization.

***Merits of Matrix Organization:***

1. In a matrix organization, all decisions are taken by experts. Therefore, the decisions give very good results.
2. It helps the employees to widen their skills. Marketing people can learn about finance and finance people can learn about marketing, etc.
3. The top managers can spend more time on strategic planning. They can delegate all the routine, repetitive and less important work to the project managers.
4. Matrix organization responds to the negative changes in the environment. This is because it takes quick decisions.
5. In a matrix organization, there is a specialization. The functional managers concentrate on the technical matters while the project manager concentrates on the administrative matters of the project.
6. The matrix organization results in a higher efficiency. It gives high returns at lower costs.

***Demerits of Matrix Organization:***

1. In a matrix organization, the operational cost is very high. This is because it involves a lot of paperwork, reports, meetings, etc.
2. In a matrix organization, there is no unity of command. This is because; each subordinate has two bosses, viz., Functional Manager and Project Manager.
3. In a matrix organization, there may be a power struggle between the project manager and the functional manager. Each one looks after his own interest, which causes conflicts.
4. In a matrix organization, the morale of the employees is very low. This is because they work on different projects at different times.
5. Matrix organization is very complex and the most difficult type of organization.

4. **Task force organization**: A task force is created by drawing personnel from various functional departments and putting them under the project manager as shown in Fig. 4.20. The staff so assigned will continue to receive administrative support from their home departments but they will respond only to the project manager while receiving all directions. Referring to the domestic matrix, the mother is supposed to concentrate on the home and the father on the career. It works in a similar manner in a project too. The functional departments provide the individuals with expertise for projects to use, and a home to return back when the expertise is not longer needed by the project.

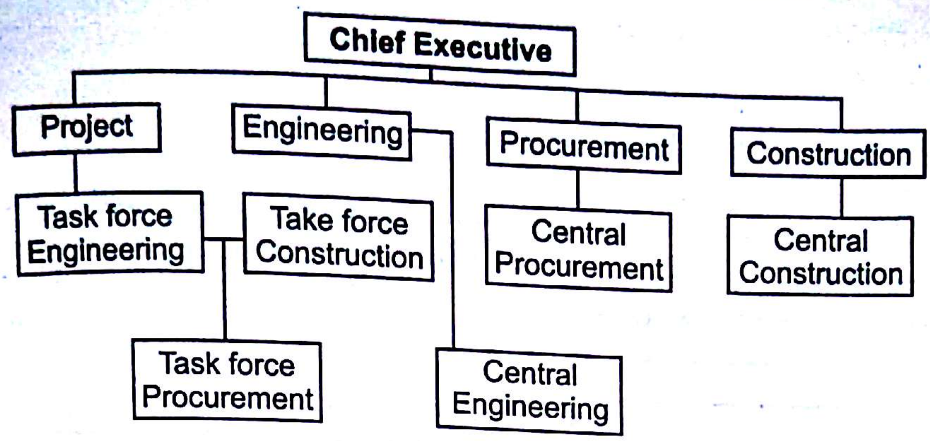


**Fig. 4.20** Task force organizations

The project merely calls for the expertise and directs its use in the best interest of the project. So the project should decide what is to be done, when it is to be done and at what budget, it should be for the functional departments to decide who should do it, what back-up he should be given, what norms and standards he should follow so that the work is completed as per specifications and within the time the budget.

5. **Divisional organizations:** Under this form of project organization, a separate division is set up to implement the project as shown Fig. 4.21. Headed by the project manager, this division has its complement personnel over whom the project manager has full authority.

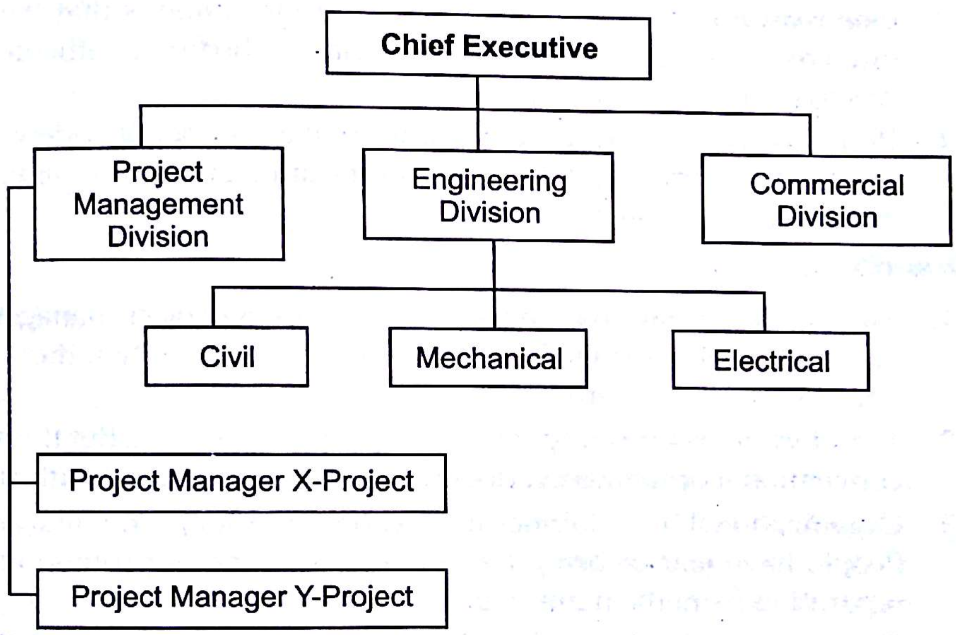


**Fig. 4.21** Divisional organizations

6. **Projected organization:** A totally projected organization is an arrangement in which the project manager has total authority even regarding functional policies and procedures as shown in Fig. 4.22. There are no constraints or limitations what so ever with respect to any function. The functional specialists have no one to notify. They will be carrying out what the project demands and the project manager instructs.

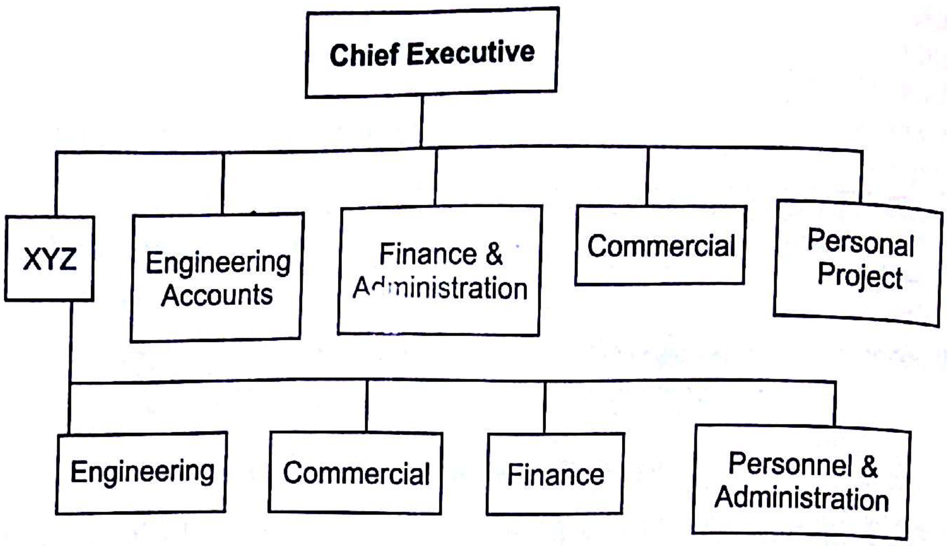


**Fig. 4.22** Projected organizations

***Merits:***

1. Project organization provides concentrated attention that a complex project demands. It permits the timely completion of a project without disturbing the normal routine of rest of the organization.
2. Project organization provides a logical approach to any challenge in the form of a large project with definite beginning, end and clearly defined result.
3. One reason for the success of project organization is that the project often requires highly talented professionals who find it difficult to work creatively in any structured set-up.
4. Project organization has been found to fit a number of widely-varying situations, from building contractors and advertising agencies to accounting and consulting firms.

***Demerits:***

1. There is organizational uncertainty because a project manager has to deal with professionals drawn from diverse fields. Often they differ in approach and interest.
2. A project manager is responsible for project outcomes. But the ongoing conventional organization does not give him unlimited authority.
3. Organizational uncertainties may lead to inter-departmental conflicts. People have fear of being forgotten at the time of promotion due to separation from the main structure.
4. There is considerable fear among personnel that the completion of a project may result loss of job.

## REVIEW QUESTIONS

1. Define project organization and explain its importance.
2. Explain BCG matrix and its implication. *(R.G.P.V., Dec. 2009)*
3. List steps in decision-making.
4. Explain the merits and demerits of divisional form of project organization.

5. What is line and staff from organization? Explain its merits. *(R.G.P.V., June. 2010)*
6. Explain relation between authorities and responsibilities. *(R.G.P.V., June. 2010)*
7. What do you meant by SWOT analysis?
8. Steps in decision making? Explain structured and unstructured decision.
9. What are the principles of organization?
10. Explain the types of organization.
11. What are the different dimensions of organizations
12. What is departmentalization? Explain its different forms.
13. Explain business process reengineering and when it is required. *(R.G.P.V., Dec. 2009)*
14. Draw a leadership grid and explain. *(R.G.P.V., June. 2010)*
15. Briefly describe different forms of project organizations.
16. What is matrix organization? Explain its significance.
17. Under which situation projected organization will hold good?
18. What is span and line of control? Explain its component.
19. Explain the following organization typology:
    (a) Line
    (b) Staff
    (c) Matrix organization
    (d) Co-ordination by task force
20. Explain the GE –McKinsey Matrix.
21. Explain Mintzberg's organization typology with a figure. Its important characteristics. *(R.G.P.V., Dec. 2009)*

# 5. Re-engineering and Process of Change Management

**Chapter Outline**



## 5.1 INTRODUCTION

In simple words, planning is deciding in advance what is to be done, when where, how and by whom it is to be done. Planning bridges the gap from where we are to where we want to go. It includes the selection of objectives, policies, procedures and programs from among alternatives. A plan is a predetermined course of action to achieve a specified goal. It is an intellectual process characterized by thinking before doing. It is an attempt on the part of manager to anticipate the future in order to achieve better performance. Planning is the primary function of management.

## 5.2 HR PLANNING

Human resource planning is a process that identifies current and future human resources needs for an organization to achieve its goals. Human resource planning should serve as a link between human resource management (HRM) and the overall strategic plan of an organization.

**Important Point:** *Human resource planning is a dynamic management process of ensuring that all times a company or its units has in its employ the right number of people with the right skills, assigned to the right jobs where they can contribute effectively to the productivity and profitability of the company.*

### 5.2.1 Features of HR Planning

Human resources planning anticipate not only the required kind and number of employees but also determine the action plan for all functions of personnel management. The major payoffs of human resources planning may be catalogued in the following way:

1. **Necessary of all organization:** Human resource planning is necessary of all organization. They cooperate companion of the organization regarding expansion, diversification, technological change, that should be backed up by the availability of human resources. It suggests suitable modification in the plan when the expected manpower is not available.
2. **Uncertainty and change:** It balances uncertainty and changes, sometime the organization may have machines and money but not men and consequently the production cannot be started. It offsets such uncertainly and changes to the maximum possible and enables the society to have right men at right time and in the right place.
3. **Advancement and development of employees:** It provides scope for advancement and development of employees through induction, training, development, etc.
4. **Satisfy the individual needs:** It helps to satisfy the individual needs of the employees for the promotions, transfers, salary enhancement, better benefits, etc.
5. **Anticipating the cost:** It helps in anticipating the cost of salary benefits and all the cost of human resources facilitating the formulation of budgets in a society.
6. **Physical facilities:** It helps in planning for physical facilities, working conditions, the volume of fringe benefits like canteen, schools, hospitals, conveyance, child care centers, residential quarters, company stores, etc.
7. **Other:** It causes the development of various sources of human resources to meet the organizational needs. It helps to take steps to improve human resource contributions in the form of increased productivity, sales, turnover, etc. It facilitates the control of all functions, operations, contribution and cost of human resources.

### 5.2.2 HR Strategy and Plans

The planning processes of most best practice organizations not only define what will be accomplished within a given period of time, but also the numbers and types of human resources that will be required to achieve the defined business goals like - number of human resources, the required competencies, when the resources will be needed, etc. The Strategic HR Planning and evaluation cycle is shown in Fig. 5.1.

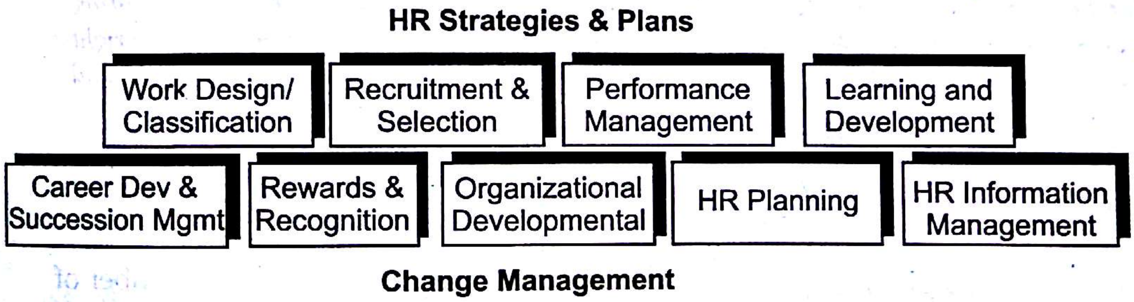


**Fig. 5.1** HR Strategy and Plans

Targeted human resource strategies, plans and programs to address gaps e.g. hiring/staffing, learning, career development, succession management, etc. are then designed developed and implemented to seal the gaps.

These strategies and programs are monitored and evaluated on a regular basis to ensure that they are moving the organizations in the desired direction, including closing employee competency gaps, and corrections are made as desired.

### 5.2.3 Objectives of HR Planning

The major objective of Human Resource Planning in an organization is to:

1. Ensure optimum use of human resources currently employed.
2. Avoid balances in the distribution and allocation of human resources.
3. Assess or forecast future skill requirements of the organization's overall objectives.
4. Provide control measure to ensure availability of necessary resources when required.
5. Control the cost aspect of human resources.
6. Formulate transfer and promotion policies.

### 5.2.4 Elements of Human Resource Planning

Human resources planning anticipate not only the required kind and number of employees but also determine the action plan for all functions of personnel management as shown in Fig. 5.2. The elements of HR are as following:

1. **Planning and Appraisal:** How an organization sets goals, plans performance, provides ongoing coaching, and evaluates performance of employees (individuals and/or teams).


Fig. 5.2 Elements of Human Resource Planning

2. **Individual and Team Development:** How an organization identifies the needs for employee skill development, education, and growth and how they meet those needs.
3. **Career Planning and Hiring:** How an organization strives to help employees to learn their strengths and to match these strengths, aptitudes, preferences, and abilities to future work. Hiring means how an organization defines and fills positions and roles with qualified people from within and/or outside the organization; how an organization orients these new employees.
4. **Career Pathing:** How an organization (for key positions and roles) determines the logical progression of jobs, roles, assignments, and development to provide a sufficient pool of qualified candidates and incumbents.
5. **Job Design and Classification:** How an organization determines the best methods for accomplishing a work product or result. The two major types are the individual job and the team. Classification is a systematic process used for evaluating the size and appropriate salary ranges for different jobs and roles in an organization.
6. **Compensation/Recognition/Other Rewards:** How an organization pays and rewards employees (individuals and/or teams), through salary, bonuses, benefits and/or non-financial rewards.

## 5.3 PLACEMENT AND TRAINING

Placement refers to assigning rank and responsibility to an individual, identifying him with a particular job. If the person adjusts to the job and continues to perform as per expectations, it means that the candidate is properly placed. However, if the candidate is seen to have problems in adjusting himself to the job, the supervisor must find out whether the person is properly placed as per the latter's aptitude and potential. Usually, placement problems arise out of wrong selection or improper placement or both. Therefore, organizations need to constantly review cases of employees below expectations/potential and employee related problems such as turnover, absenteeism, accidents etc., and assesses how far they are related to inappropriate placement decisions and remedy the situation without delay.

Placement is a process of gathering information for the purposes of evaluating and deciding who should be employed or hired for the short and long-term interests of the individual and the organization.

**Important Point:** *Placement is a process of assigning a specific job to each of the selected candidates. It involves assigning a specific rank and responsibility to an individual. It implies matching the requirements of a job with the qualifications of the candidate.*

In other words it is the process of getting the best of most qualified candidates from the pool of job seekers adjudged to have potential for job performance. The significances of placement are as follows:

1. It improves employee morale.
2. It helps in reducing employee turnover.
3. It helps in reducing absenteeism.
4. It helps in reducing accident rates.
5. It avoids misfit between the candidate and the job.
6. It helps the candidate to work as per the pre-determined objectives of the organization.

Training is the achievement of knowledge and skills as a result of the teaching of vocational or practical skills and knowledge that relate to specific useful competencies. Training has specific goals of improving one's capability, capacity, and performance.

### 5.3.1 Objectives of Training

The objectives for the training of employees:

1. **Increase productivity:** Instructions can help employees increase their level of performance on their present assignment. Increased human performance often leads to increased operational productivity and increased company profit.
2. **Improve quality**: Better informed worked are less likely to make operational mistakes. Quality increases may be in relationship to company product or service or in reference to the intangible organizational employment atmosphere.
3. **Personal growth**: Employees on a personal basis gain individually from their exposure to educational expressions. Management development program seems to give participants a wider awareness, an enlarged skill and enlightens realistic philosophy and make personal growth possible.
4. **To help a company fulfill its future personnel needs**: Organizations that have a good internal program for development need to make less extreme manpower changes and adjustments in the event of sudden personnel alterations. When the need arises organizational vacancies can be easily staffed from maintaining an adequate instructional program for both its non-supervisory and managerial employees.
5. **Improve organizational climate**: An endless chain of positive reactions result from a well planned training program.
6. **Improve health and safety**: Proper training can help prevent industrial accidents. A safer atmosphere leads to more stable mental attitudes on part of employees. Managerial mental status would also improve, if supervisors know they can better themselves through company designed development programs.

## 5.4 MANAGEMENT INFORMATION SYSTEM (M.I.S)

The management information system (MIS) is a concept of the last decade or two. It is also known as the information system, the information and decision system, the computer- based information system. The MIS has more than one definition, some of which are give below.

**Important Point:** *The MIS is defined as a system which provides information support for decision making in the organization.*

- *The MIS is defined as an integrated system of man and machine for providing the information to support the operations, the management and the decision making function in the organization.*
- *The MIS is defined as a system based on the database of the organization evolved for the purpose of providing information to the people in the organization.*
- *The MIS is defined as a computer based information system.*

Information systems and MIS are broader categories that include enterprise resource planning (ERP). Information technology management concerns the operation and organization of information technology resources independent of their purpose, Decision support system (DSS), executive information system, etc. as shown in Fig. 5.3.

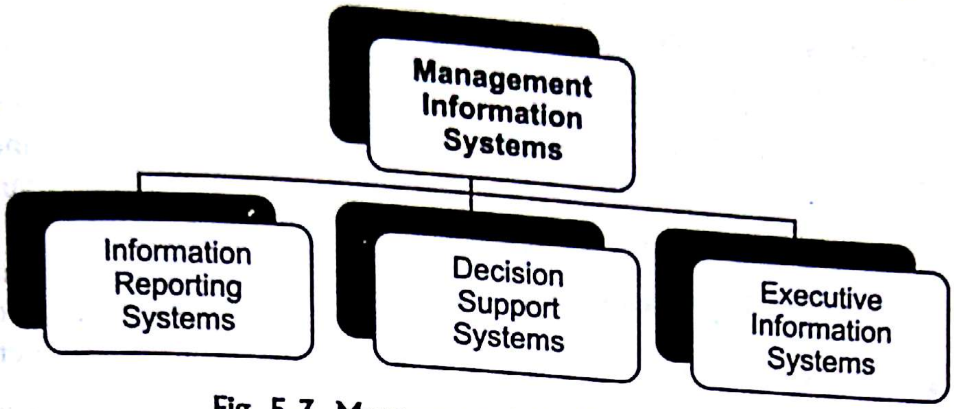


Fig. 5.3 Management Information System

### 5.4.1 Role of the Management Information System

The role of the MIS in an organization can be compared to the role of heart in the body. The information is the blood and MIS is the heart. In the body the heart plays the role of supplying pure blood to all the elements of the body including the brain. The heart works faster and supplies more blood as and when needed. It regulates and controls the incoming impure blood, processes it and sends it to the destination in the quantity needed. It fulfills the needs of blood supply to human body in normal course and also in crisis.

1. The MIS plays exactly the same role in the organization. The system ensures that an appropriate data is collected from the various sources, processed, and sent further to all the needy destinations.
2. The system is expected to fulfill the information needs of an individual, a group of individuals, the management functionaries: the managers and the top management.
3. The MIS satisfies the diverse needs through a variety of systems such as Query Systems, Analysis Systems, Modeling Systems and Decision Support Systems (DSS). The MIS also helps in Strategic Planning, Management Control, Operational Control and Transaction Processing.
4. The MIS helps the clerical personnel in the transaction processing and answers their queries on the data pertaining to the transaction, the status of a particular record and references on a variety of documents.
5. The MIS helps the junior management personnel by providing the operational data for planning, scheduling and control.

### 5.4.2 Advantages of MIS

The following are some of the benefits that can be attained for different types of management information systems:

1. Companies are able to highlight their strengths and weaknesses due to the presence of revenue reports, employees' performance record etc. The

identification of these aspects can help the company to improve their business processes and operations.

2. Giving an overall picture of the company and acting as a communication and planning tool.
3. The availability of the customer data and feedback can help the company to align their business processes according to the needs and wants of the customers. The effective management of customer data can help the company to perform direct marketing and promotion activities.
4. Information is considered to be an important asset for any company in the modern competitive world. The consumer buying trends and behaviours can be predicted by the analysis of sales and revenue reports from each operating region of the company.

## 5.5 ATTITUDE

Attitude plays an important role in improving the relationship among the individuals. Nothing is possible until and unless an individual has a positive attitude towards life. You might have excellent communication skills, might be an intelligent worker, but if you do not have a positive attitude; you would definitely fail to create an impression of yours. People would be reluctant to speak to you and you would be left all alone.

**Important Point**: *"A psychological tendency that is expressed by evaluating a particular entity with some degree of favor or disfavor".* *-Eagly & Chaiken,*

- *An attitude is a relatively enduring organization of beliefs, feelings, and behavioural tendencies towards socially significant objects, groups, events or symbols.*

### 5.5.1 Structure of Attitudes

Attitudes structure can be described in terms of three components called ABC model as shown in Fig. 5.4. This model is known as the **ABC model of attitudes.** The three components are usually linked.

(i) **Affective component (A)**: This involves a person's feelings/emotions about the attitude object. For example: "I am scared of lizards".

(ii) **Behavioural component (B)**: The way the attitude we have influences how we act or behave. For example: "I will avoid lizards and scream if I see one".

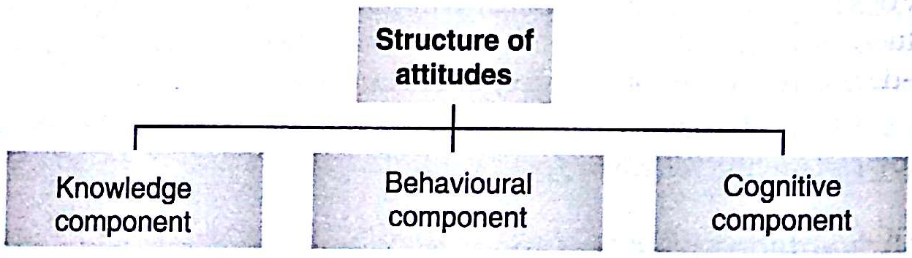


Fig. 5.4 ABC model

(iii) **Cognitive component (C)**: This involves a person's belief/knowledge about an attitude object. For example: "I believe lizards are dangerous".

However, there is evidence that the cognitive and affective components of behaviour do not always match with behaviour.

### 5.5.2 Function of Attitudes

Attitudes can serve functions for the individual outlines four functional areas as shown in Fig. 5.5:

*(i)* **Knowledge:** Attitudes provide meaning (knowledge) for life. The knowledge function refers to our need for a world which is consistent and relatively stable. This allows us to **predict** what is likely to happen, and so gives us a sense of control. Attitudes can help us organize and structure our experience. Knowing a person's attitude helps us to predict their behaviour. For example, knowing that a person is religious we can predict they will go to temple.

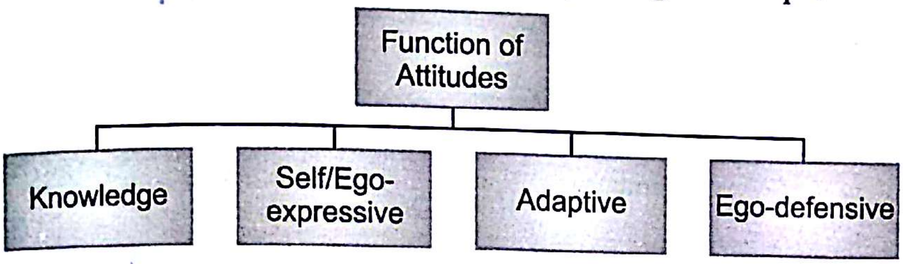


**Fig. 5.5** Function of Attitudes

*(ii)* **Self/Ego-expressive:** The attitudes we express (1) help **communicate** who we are and (2) may make us feel good because we have asserted our identity. Self-expression of attitudes can be non-verbal too: think bumper sticker, cap, or T-shirt slogan. Therefore, our attitudes are part of our identify, and help us to be aware through expression of our feelings, beliefs and values.

*(iii)* **Adaptive:** If a person holds and or expresses socially acceptable attitudes, other people will reward them with approval and **social acceptance**. For example, when people flatter their bosses or instructors (and believe it) or keep silent if they think an attitude is unpopular.

*(iv)* **Ego-defensive:** This function refers to holding attitudes that **protect** our self-esteem or that justify actions that make us feel guilty. For example, one way children might defend themselves against the feelings of humiliation they have experienced in physical education lessons is to adopt a strongly negative attitude to all sport. People whose pride has suffered following a defeat in sport might similarly adopt a defensive attitude: "I' am not bothered, I am sick of rugby anyway...". This function has psychiatric overtones. Positive attitudes towards ourselves, for example, have a protective function (*i.e.*, an ego-defensive role) in helping us reserve our self-image.

## 5.6 PERSONALITY TRAIT

An individual's behaviour toward others attitude, characteristics, mindset make his personality. Personality development is defined as a process of enhancing one's personality.

Broadly there are five parameters which describe an individual's personality as shown in Fig. 5.6. These five categories are usually described as follows as shown in Fig. 5.6:

1. **Extraversion:** This trait includes characteristics such as excitability, sociability, talkativeness, assertiveness and high amounts of emotional expressiveness.
2. **Agreeableness:** This personality dimension includes attributes such as trust, humanity, kindness, affection, and other prosaically behaviours.

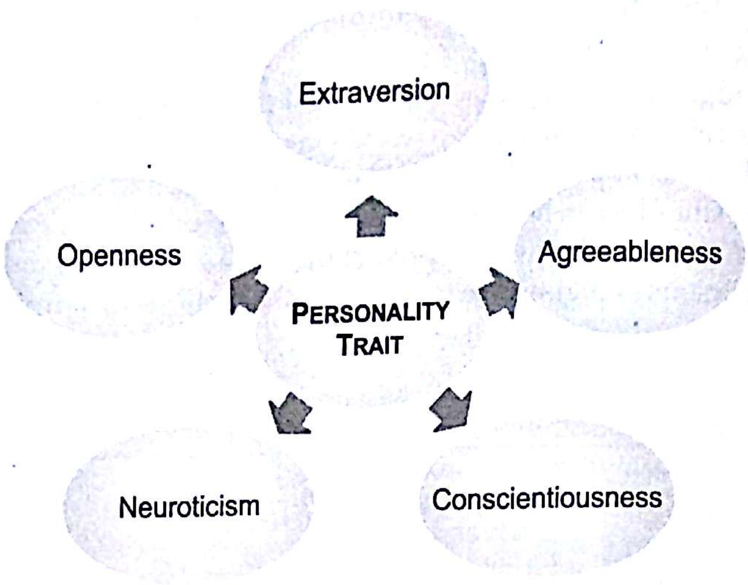


**Fig. 5.6** Personality Trait

3. **Conscientiousness:** Common features of this dimension include high levels of thoughtfulness, with good impulse control and goal-directed behaviours. Those high in conscientiousness tend to be organized and mindful of details.
4. **Neuroticism:** Individuals high in this trait tend to experience emotional instability, anxiety, moodiness, irritability, and sadness.
5. **Openness:** This trait features characteristics such as imagination and insight, and those high in this trait also tend to have a broad range of interests.

### 5.6.1 Types of Personality Traits

There are many different personality types, and it is sometimes difficult to classify a person into a single type as there are many different personality traits a person can possess. Personality traits are simply:

- Actions
- Attitudes
- Behaviours that a person possess

**(i) Positive Personality Traits:** Some personality traits are positive:

- Being honest no matter what the consequences are is one personality trait people should aspire to.
- Having responsibility for all of your actions and being a little bit of perfectionism are also personality traits.
- Adaptability and compatibility are great and help you get along with others.
- Having the drive to keep going, and having compassion and understanding are positive personality traits.

- Patience is a virtue and also another trait.
- Getting up the courage to do what's right in those tough situations and loyalty to your friends and loved ones are also personality traits. Here's a few more to consider:
  - ⇒ Adventurous
  - ⇒ Affable
  - ⇒ Cultured
  - ⇒ Dependable
  - ⇒ Fair
  - ⇒ Fearless
  - ⇒ Observant
  - ⇒ Independent
  - ⇒ Optimistic
  - ⇒ Intelligent
  - ⇒ Keen
  - ⇒ Gregarious (Sociable)
  - ⇒ Capable
  - ⇒ Charming
  - ⇒ Confident
  - ⇒ Dutiful
  - ⇒ Encouraging
  - ⇒ Reliable
  - ⇒ Enthusiastic
  - ⇒ Helpful
  - ⇒ Humble
  - ⇒ Imaginative
  - ⇒ Obedient
  - ⇒ Trusting

**(ii) Negative Personality Traits:** Other personality traits are negative. For example:

- ⇒ Laziness
- ⇒ Picky
- ⇒ Pompous
- ⇒ Dishonesty
- ⇒ Arrogant
- ⇒ Cowardly
- ⇒ Sneaky
- ⇒ Rude
- ⇒ Argumentative
- ⇒ Careless
- ⇒ Abrupt

⇒ Unfriendly
⇒ Disobedient
⇒ Stingy
⇒ Dominant

A whole host of other bad characteristics can also be considered personality traits if you practice these things habitually.

## 5.7 DIFFERENCES BETWEEN MANAGER & LEADER

Leadership differs from management in a sense that:

| S.No. | Management | Leadership |
|---|---|---|
| 1. | Managers lay down the structure and delegates authority and responsibility. | A leader provides direction by developing the organizational vision and communicating it to the employees and inspiring them to achieve it. |
| 2. | It includes focus on planning, organizing, staffing, directing and controlling. | Leaders focus on listening, building relationships, teamwork, inspiring, motivating and persuading the followers. |
| 3. | Manager gets his authority by virtue of his position in the organization. | Leader gets his authority from his followers. |
| 4. | Managers follow the organization's policies and procedure. | Leaders follow their own instinct. |
| 5. | Management is more of science as the managers are exact, planned, standard, logical and more of mind. | Leadership, on the other hand, is an art. In an organization, if the managers are required, then leaders are a must/essential. |
| 6. | Management deals with the technical dimension in an organization or the job content. | Leadership deals with the people aspect in an organization. |
| 7. | Management measures/evaluates people by their name, past records and present performance. | Leadership sees and evaluates individuals as having potential for things that can be measured, *i.e.*, it deals with future and the performance of people if their potential is fully extracted. |
| 8. | Management is reactive. | Leadership is proactive. |
| 9. | Management is based more on written communication. | Leadership is based more on verbal communication. |

## 5.8 LEADERSHIP GRID

**Robert Blake and Jane Mouton (1960s)** proposed a graphic depiction of leadership styles through a managerial grid sometimes called leadership grid for building on the work of the researchers at these universities. The grid depicted two dimensions of leader behaviour, concern for people on y-axis and concern for production (keeping tight schedules) on x-axis. The dimension ranging from low (1) to high (9), thus creating 81 different positions in which the leader's style may fall as shown in Fig. 5.7.

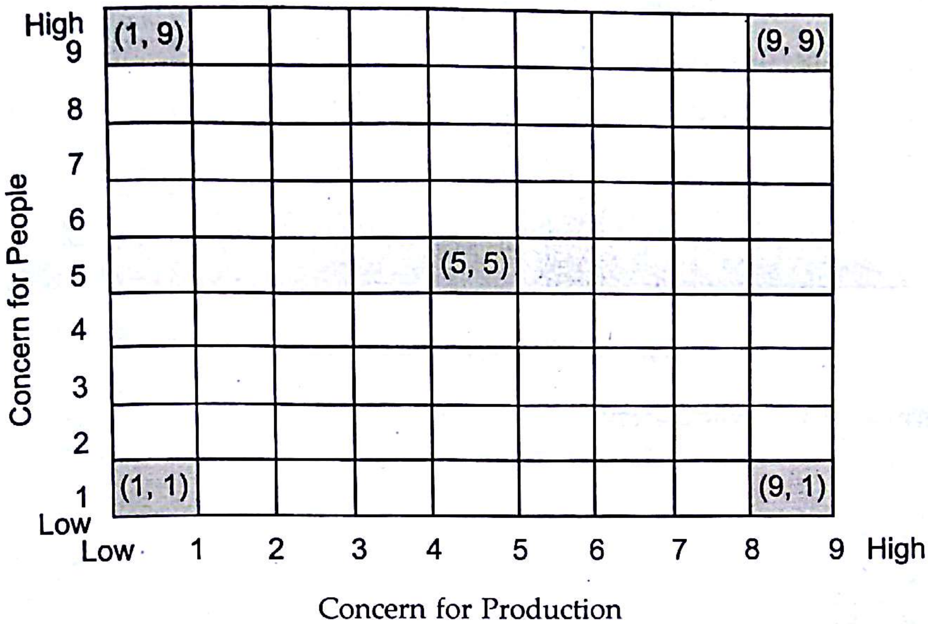


**Fig. 5.7** Leadership Grid

The five resulting leadership styles are as follows:

1. **Impoverished (Poor) Management (1, 1):** Managers with this approach are low on both the dimensions.
2. **Task management (9, 1):** Here leaders are more concerned about production and have less concern for people. The employees' needs are not taken care of and they are simply a means to an end.
3. **Middle-of-the-Road (5, 5):** Here neither employee nor production needs are fully met.
4. **Country Club (1, 9):** Here the leader gives thoughtful attention to the needs of people thus providing them with a friendly and comfortable environment but are less concern of production exists.
5. **Team Management (9, 9):** Here the leader feels that empowerment, commitment, trust, and respect are the key elements in creating a team atmosphere which will automatically result in high employee satisfaction and production.

## 5.9 MASLOW'S NEED HIERARCHY

**Maslow** defined a Hierarchy of Human Needs that stated the lower needs must be met before an individual can strive to meet the higher needs. "According to

Maslow's theory, all needs have a certain priority. Needs of one level must at least partially fulfilled before a person can realize higher needs" as shown in Fig. 5.8.

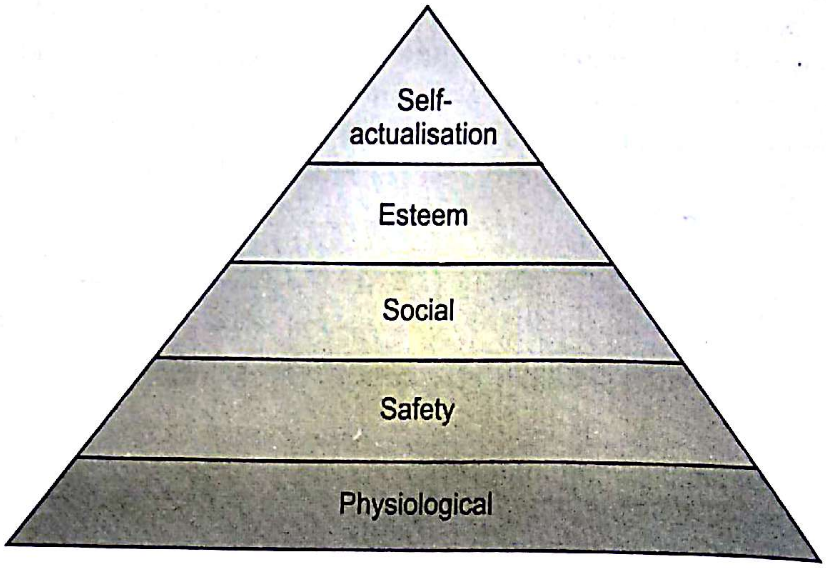


Fig. 5.8 Maslow's Need Hierarchy

(i) **Physiological Needs**: These are necessary and essential needs of human being for life to be met. If these needs are not fulfilled it may lead to death. Some the example of these need are:
- Food
- Clothing
- Shelter

(ii) **Safety**: Safety needs have to do with establishing stability and consistency in this world. We need the security of a home and family. Safety needs sometimes motivate people to be religious. Religions comfort us with the promise of a safe secure place after we die and leave the insecurity of this world.

(iii) **Social (Love and belonging)**: Love and belongingness are next on the hierarchy. Humans have a desire to belong to groups: clubs, work groups, religious groups, family, society, etc. We need to feel loved (non-sexual) by others, to be accepted by others.

(iv) **Esteem Needs**: There are two types of esteem needs.
- First is self-esteem which results from competence or mastery of a task.
- Second, there is the attention, recognition and respect that come from others.

This is similar to the belongingness level; however, wanting admiration has to do with the need for power.

(v) **Self-Actualization**: The need for self-actualization is the "desire to become more and more what one is, to become everything that one is capable of becoming." People who have everything can maximize their potential. **Example**— Working for an NGO.

## 5.10 HERZBERG TWO FACTOR THEORY

In 1959, **Frederick Herzberg**, a behavioural scientist proposed a two-factor theory or the motivator-hygiene theory. **According to Herzberg, the opposite of**

**"Satisfaction" is "No satisfaction" and the opposite of "Dissatisfaction" is "No Dissatisfaction".**

> *There are some job factors that result in satisfaction while there are other job factors that prevent dissatisfaction.*
>
> *-Herzberg*

According to the Two-Factor theory a distinction has to be made in the workplaces between motivators and hygeine factors as shown in Fig. 5.9.

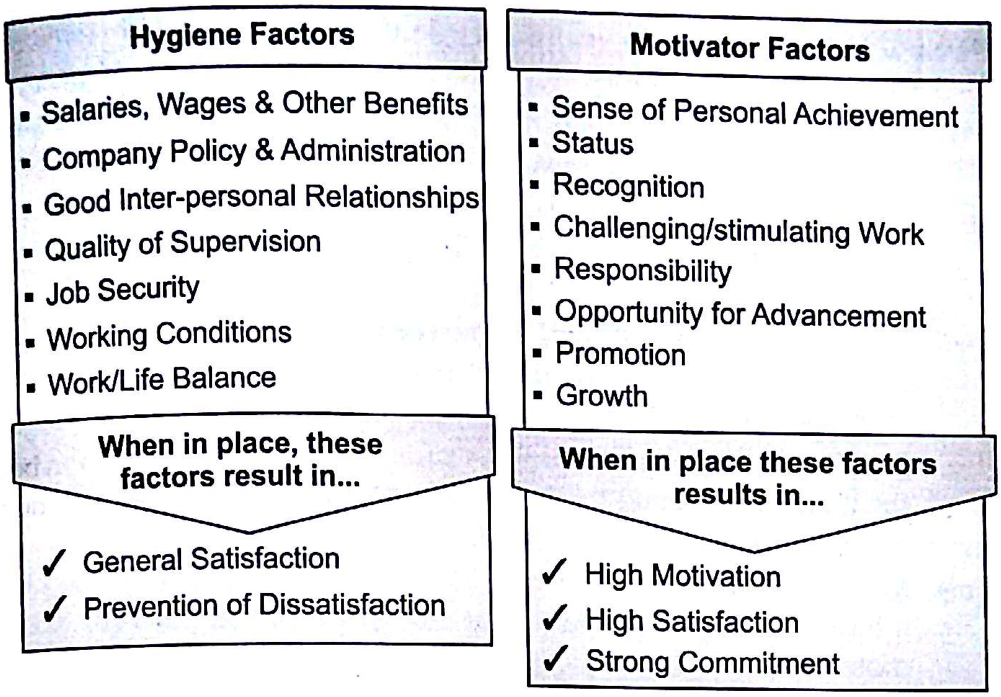


**Fig. 5.9** Frederick Herzberg Two Factor

1. **Hygiene factors:** These are essential in the work palaces in order for the employees not to be dissatisfied, at the same time, when these factors do not cause satisfaction.

   Hygiene factors include:

   (i) **Pay:** The pay or salary structure should be appropriate and reasonable. It must be equal and competitive to those in the same industry in the same domain.

   (ii) **Company Policies and administrative policies:** The company policies should not be too rigid. They should be fair and clear. It should include flexible working hours, dress code, breaks, vacation, etc.

   (iii) **Fringe benefits:** The employees should be offered health care plans (medi-claim), benefits for the family members, education for children, residential facility, low interest loans, employee help programs, etc.

   (iv) **Physical Working conditions:** The working conditions should be safe, clean and hygienic. The work equipments should be updated and well-maintained.

   (v) **Status:** The employees' status within the organization should be familiar and retained.

(vi) **Interpersonal relations:** The relationship of the employees with his peers, superiors and subordinates should be appropriate and acceptable. There should be no conflict or humiliation element present.

(vii) **Job Security:** The organization must provide job security to the employees. There should not be any fear of redundancy (being without a job).

2. **Motivators factor:** Motivators cause the employees to enhance the level of their performance and effectiveness in the work place. The motivators symbolized the psychological needs that were perceived as an additional benefit. Motivational factors include:

   (*i*) **Recognition:** The employees should be praised, appreciated and recognized for their accomplishments by the managers or superiors.

   (*ii*) **Sense of achievement:** The employees must have a sense of achievement. This depends on the job. There must be a reward of some kind in the job.

   (*iii*) **Growth and promotional opportunities:** There must be growth and advancement opportunities in an organization to motivate the employees to perform well.

   (*iv*) **Responsibility:** The employees must hold themselves responsible for the work. The managers should give them ownership of the work. They should minimize control but retain accountability.

   (*vi*) **Meaningfulness of the work:** The work itself should be meaningful, interesting and challenging for the employee to perform and to get motivated.

### 5.10.1 Limitations of Two-Factor Theory

The two factor theory is not free from limitations:

1. The two-factor theory overlooks situational variables.
2. Herzberg assumed a correlation between satisfaction and productivity. But the research conducted by Herzberg stressed upon satisfaction and ignored productivity.
3. The theory's reliability is uncertain. Analysis has to be made by the raters. The raters may spoil the findings by analyzing same response in different manner.
4. No comprehensive measure of satisfaction was used. An employee may find his job acceptable despite the fact that he may hate/object part of his job.
5. The two factor theory is not free from bias as it is based on the natural reaction of employees when they are enquired the sources of satisfaction and dissatisfaction at work. They will blame dissatisfaction on the external factors such as salary structure, company policies and peer relationship. Also, the employees will give credit to themselves for the satisfaction factor at work.
6. The theory ignores blue-collar workers. Despite these limitations, Herzberg's two-factor theory is acceptable broadly.

## 5.11 Theory X, Theory Y and Theory Z

In 1960, **Douglas McGregor** formulated Theory X and Theory Y suggesting two

aspects of human behaviour at work, or in other words, two different views of individuals (employees): one of which is negative, called as Theory X and the other is positive, so called as Theory Y. According to McGregor, the perception of managers on the nature of individuals is based on various assumptions. The following Fig. 5.10 represents - Theory X, Theory Y and Theory Z.

1. **Theory X ('Authoritarian management' style)**: This states that the average person dislikes work and will avoid it if he or she can. Therefore, most people must be forced with the threat of punishment to work towards organizational objectives. The average person prefers to be directed; to avoid responsibility; is relatively unambitious, and wants security above all. Theory X managers are facts and figures orientated-so cut out the incidentals-and want to measure and substantiate anything you say and do for them, especially reporting on results and activities. They generally do not understand or have an interest in the human issues, so there is no point in trying to appeal to their sense of humanity or morality.

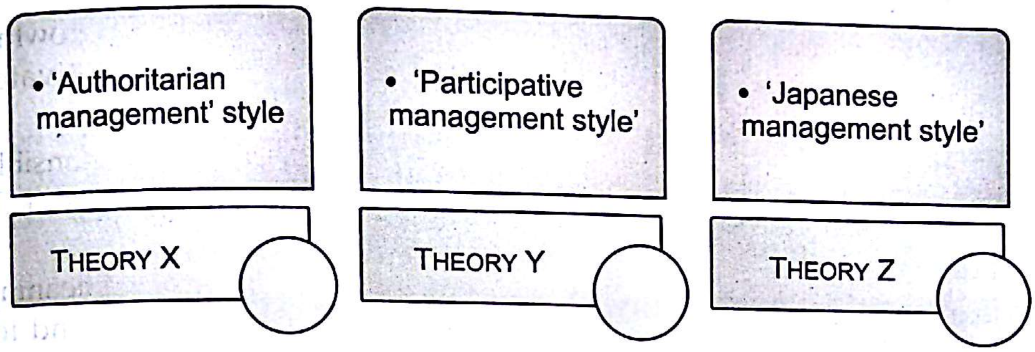


**Fig. 5.10** Theory X, Theory Y and Theory Z

2. **Theory Y ('Participative management' style)**: This states that effort in work is as natural as effort in play and that people will apply self-control and self-direction effort in the pursuit of organizational objectives, without external control or the threat of punishment. Commitment to objectives is a function of rewards associated with their achievement. People usually accept and often seek responsibility. The capacity to use a high degree of imagination, ingenuity and creativity in solving organizational problems is widely, not narrowly, distributed in the population. In industry the intellectual potential of the average person is only partly utilized and the Theory Y manager will attempt to bind and set free this ability.

3. **Theory Z ('Japanese management' style)**: Theory Z is a name applied to three distinctly different psychological theories. One was developed by **Abraham H. Maslow** in his paper Theory Z and the second is **Dr. William Ouchi's** so-called "Japanese Management" style popularized during the Asian economic boom of the 1980s. The third was developed by **W. J. Reddin** in Managerial Effectiveness.

   This essentially advocates a combination of all that's best about Theory Y and modern Japanese management, in that it places a large amount of freedom and trust in workers, and assumes that workers have a strong loyalty and interest in team-working and the organization.

## 5.12 EXPECTATION THEORY

The expectancy theory was proposed by **Victor Vroom** of Yale School of Management in 1964. This theory is a model of behavioural choice as an explanation of why individuals choose one behavioural option over others. In doing so, it explains the behavioural direction process. It does not attempt to explain what motivates individuals but rather how they make decisions to achieve the end they value. Expectancy theory is made up with of three components: Expectancy, Instrumentality, and Valance as shown in Fig. 5.11.

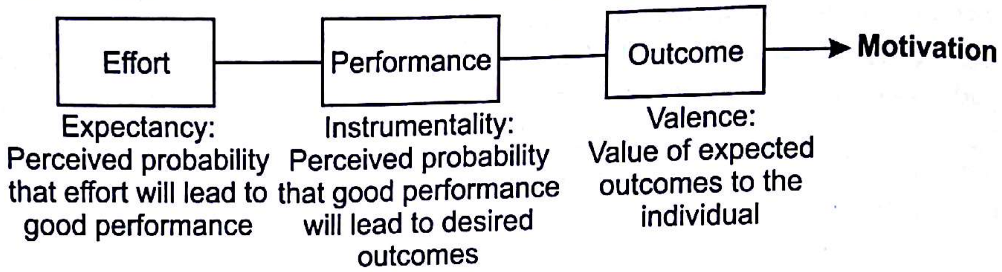


**Fig. 5.11** Expectation Theory

(*i*) **Expectancy- Probability (E→P)**: The effort (E) wills the result of desired performance (P) goals. This belief is generally based on an individual's past experience, self confidence and the perceived difficulty of the performance standard or goal.

(*ii*) **Instrumentality- Probability (P→R)**: The instrumentality is performance expectations receive a greater reward. This reward may come in the form of a pay increase, fringe benefits, promotion, recognition or sense of accomplishment.

(*iii*) **Valance. (V→R)**: Valence is the significance associated by an individual about the expected outcome. It is an expected and not the actual satisfaction that an employee expects to receive after achieving the goals.

### 5.12.1 Advantages of the Expectancy Theory

- This theory is based on self-interest individual who want to achieve maximum satisfaction and who wants to minimize dissatisfaction.
- It is stresses upon the expectations and perception; what is real and actual is immaterial.
- This emphasizes on rewards or pay-offs.
- It focuses on psychological extravagance where final objective of individual is to attain maximum pleasure and least pain.

### 5.12.2 Disadvantages of the Expectancy Theory

- The theory seems to be idealistic because quite a few individuals perceive high degree correlation between performance and rewards.
- The application of expectancy theory is limited as reward which is not directly correlated with performance in many organizations. It is also related to other parameters such as position, effort, responsibility, education, etc.

## 5.13 ERG (EXISTENCE, RELATEDNESS & GROWTH)

The ERG Theory of Clayton P. Alderfer is a model that appeared in 1969. In a reaction to the famous Hierarchy of Needs by Maslow, Alderfer distinguishes three categories of human needs that influence worker's behaviour; existence, relatedness and growth. In this theory ERG categories are as shown in Fig. 5.12:

(i) **Existence Needs:** Physiological and safety needs (such as hunger, thirst and sex). The first two levels of Maslow.

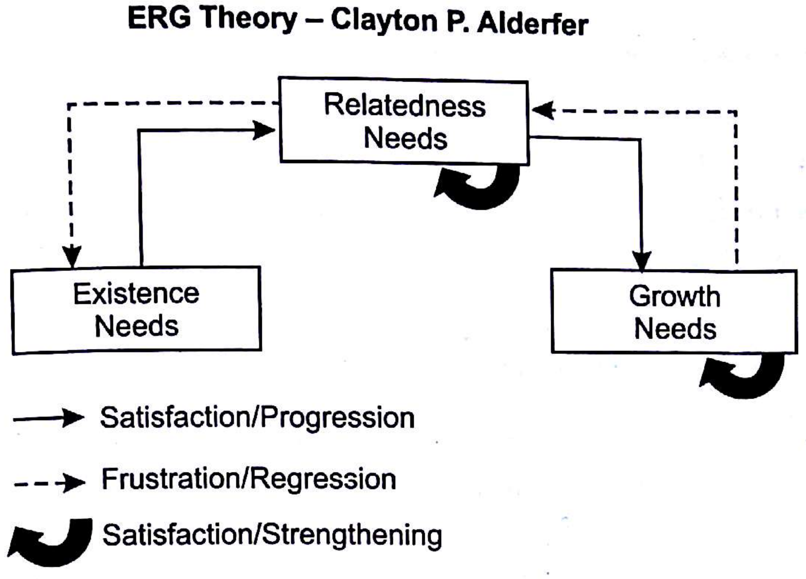


Fig. 5.12 ERG Theory

(ii) **Relatedness needs:** Social and external esteem are involvement with family, friends, co-workers and employers. They are in the third and fourth levels of Maslow.

(iii) **Growth needs:** Internal esteem and self actualization are the desire to be creative, productive and to complete meaningful tasks. Maslow's fourth and fifth levels.

ERG theory acknowledges that if a higher level need remains unfulfilled, the person may regress to lower level needs that appear easier to satisfy. This is known as the frustration-regression principle. This frustration-regression principle impacts workplace motivation. For example, if growth opportunities are not provided to employees, they may regress to relatedness needs, and socialize more with co-workers. If management can recognize these conditions early, steps can be taken to satisfy the frustrated needs until the subordinate is able to pursue growth again.

## 5.14 LEARNING PROCESS

Learning involves gaining of new behaviour. It is a kind of change in a pattern of behaviour. The individual has to learn new ways of doing things as well as new ways of thinking and feeling as he tries to adjust within his environment and to make himself useful.

**Important Point:** *"Learning can be defined as changing one's potential for seeing, feeling and doing through experiences partly perceptual, partly intellectual and partly emotional."*
*-G.M Wingo and W.C.Morse*

Learning is also dependent upon one's inherent intelligence and other capacities. It is on the basis of hereditary endowment that one can learn different types of activities and behaviour patterns. Thus the basis of learning is an individual's innate and hereditary capacities including intelligence and temperament.

### 5.14.1 Types of learning process

Learning process occurs in four major ways--transmission, acquisition, accretion and emergence as shown in Fig. 5.13.

1. **Transmission:** It is the process by which information, knowledge, ideas and skills are taught to others through purposeful, conscious telling, demonstration, and guidance.

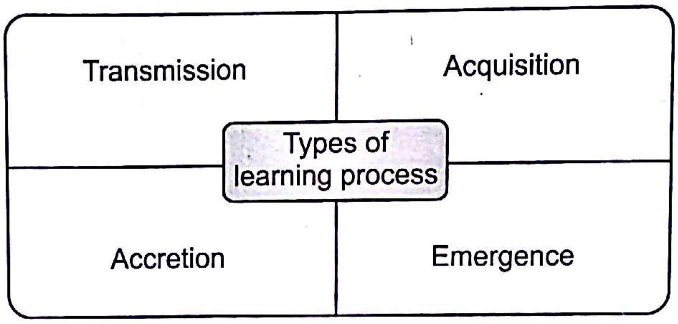


**Fig. 5.13** Types of Learning Process

2. **Acquisition:** It is the conscious choice to learn. Material in this category is relevant to the learner. This method includes exploring, experimenting, self-instruction, inquiry, and general curiosity.
3. **Accretion:** It is the gradual, often sub-conscious or hidden process by which we learn things like language, culture, habits, prejudices, and social rules and behaviours.
4. **Emergence:** This is the result of patterning, structuring and the construction of new ideas and meanings that did not exist before, but which emerges from the brain through thoughtful reflection, insight and creative expression or group interactions.

## 5.15 TEAM WORK

In one medium sized organization, formal management responsibilities being assigned to teams of people from different parts of the organization. Instead of having formal positions for specific functions (human resources, health and safety, etc.), a committee structure has been created and successfully implemented. This helps ensure that the responsibility and accountability for these important functions is shared between a numbers of people.

**Important Point:** *A team is defined as a group of people working together to achieve common objectives or goals.*

- *Teamwork is the cumulative actions of the team during which each member of the team subordinates his individual interests and opinions to fulfill the objectives or goals of the group.*

Team work is essential because: Many processes of the organization are so complex that one person cannot be knowledgeable concerning the entire process. Second, the whole is greater than the sum of its members. The interaction within the team produces results that exceed the contribution of each member. Third, team members develop a rapport with each other than allows them to do better job.

### 5.15.1 Features of Team Work

1. Members of a team will need to focus on how they relate to each other, listen to the suggestions of others, build on previous information and use conflict creatively.
2. They will need to set standards, maintain discipline, build team spirit and motivate each other.
3. Each member of the team has their own history of experience to help achieve the objectives.
4. Teams work because many heads are more knowledgeable than one. Each member of the team has special abilities and skills that can be use to solve problems.
5. Finally, team provides the vehicle for improved communication, thereby increasing the likelihood of a successful solution.

### 5.15.2 Types of Teams

They may be called by different names and slightly different characteristics to accommodate a particular organization as shown in Fig. 5.14.

1. **Process improvement teams:** The members of the process improvement team represent each operation of the process or sub-process. Usually th...

the team's activity is limited to the work unit. Process improvement in any organization is difficult when the tasks for improving processes get assigned to supervisors and the priority for them is to get the job done first and improve things later. The process improvement team helps to alleviate this type of problem and also gives empowerment to more of the people that are actually performing the jobs.

2. **Cross functional teams:** A team about six to ten members will represent a number of different functional areas, such as engineering, marketing, accounting, production, quality and human resources. It may also include the customer and supplier.

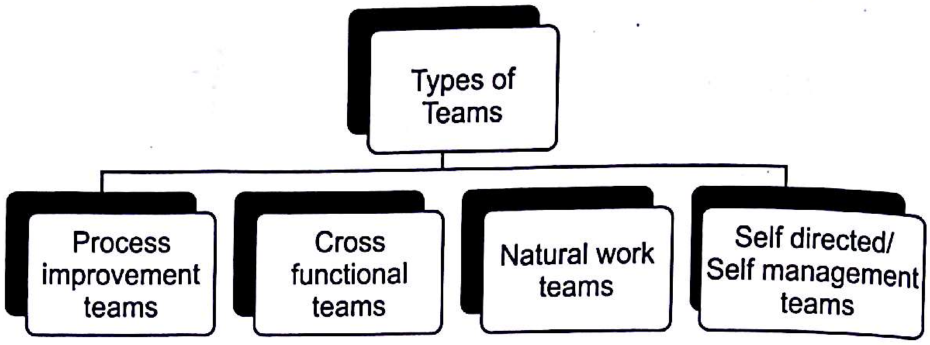


**Fig. 5.14** Types of Teams

3. **Natural work teams:** This type of team is now voluntary–it is composed of all the members of the work unit. It differs from quality control circles because a manager is a part of the team and the projects to be improved are selected by management. Some employees may not like to work in teams for various reasons and managers should anticipate this action and be prepared to help employees become comfortable in the team environment or alternatively find work in another unit that still performs work as individuals.

4. **Self directed/Self management teams:** They are an extension of natural work teams without the supervisor. Thus, they are the personification of the empowered organization–they not only do the work but also manage it.

## 5.16 STRESS MANAGEMENT

In today's changing and competitive work environment, stress level is increasing both in the workers as well as the managers.

**Important Point:** *"Stress is defined as an adaptive response to an external situation that results in physical, psychological and/or behavioural deviations, for organizational participants."*

*"Job stress is a condition arising from the interaction of the people and their jobs, and characterized by changes within people that force them to deviate from their normal functioning."*

*-Beehr and Newman*

*"Stress is a dynamic condition in which an individual is confronted with an opportunity, constraints or demand related to what he or she desires and for which the outcome is perceived to be both uncertain and important."*

### 5.16.1 Stress Management Techniques

In very simple words, stress refers to an individual's reaction to a disturbing factor in the environment. The following Fig. 5. 15, showed the stress management techniques:

1. **Accept those things that you cannot change:** Identify the stressful things in life that cannot be influenced and changed. Recognize that there is no point in worrying about things that one cannot change. Understanding this can help reduce disappointment and bitterness when things do not turn out the way we were hoping.

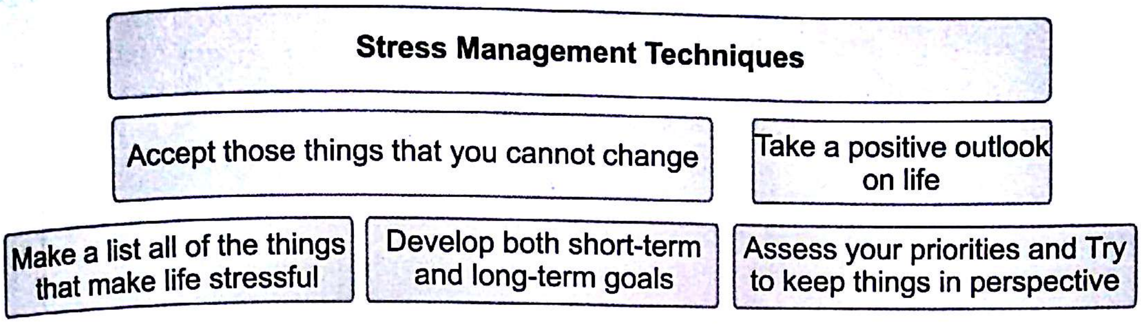


Fig. 5.15 Stress Management Techniques

2. **Take a positive outlook on life:** Learn from your mistakes, but always focus on the positives in life. A positive attitude attracts a positive energy, allowing you to be better prepared for life's challenges and stresses.
3. **Make a list all of the things that make life stressful** and a list of things that would make life less stressful. Work on strategies to change what you can do for reducing the stressful elements of life and introducing more of the stress relief elements.
4. **Develop both short-term and long-term goals** to focus your life. Goals, aspirations and priorities help to increase energy and motivation. Remember to take into consideration the amount of stress that these goals will incur and identify ways to reduce these stresses on the way to achieving your goals.
5. **Assess your priorities** and the balance between your professional, family and social life.
6. **Try to keep things in perspective** and do not put too much pressure on yourself to succeed. Ambition is a incredible motivator, however we all have bad days and something things do not turn out how we expected. Keeping your priorities in perspective can help to reduce stress and pressure.

## Review Questions

1. What is motivation? Explain maslow herzberg theories. *(R.G.P.V., Dec. 2009)*
2. What do you understand by change management?
3. Explain HR-Planning and its objectives.
4. Define MIS and its role in an organization.
5. What do mean by attitude and personality.
6. Explain managerial grid in leadership.

7. Explain in detail the Maslow's need hierarchy theory. How does it differ from the Herzberg's two factor theory'?
8. Explain clearly Vroom's expectancy theory.
9. Describe the concept of organization structure. What are the needs for organization structure? *(R.G.P.V., June 2010)*
10. What are Theory X, Theory Y and Theory Z.?
11. Explain the ERG (Existence, Relatedness & Growth) with example.
12. Explain the following:
    (a) Team work
    (b) Learning process
    (c) Stress management

# 6 Marketing Plan

## Chapter Outline



## 6.1 INTRODUCTION

Marketing management is a broad scope of the study of marketing focusing on the practical application of the techniques and marketing activities of a certain company or business. This business discipline encompasses marketing planning and strategy, orientations, and processes needed in attaining company goals by providing value to clients. Since it has a wide coverage involving all factors required to satisfy customers, marketing management must be all-pervasive and part of every employee's scope of work, from the subordinates to those in the higher management. If we look at this definition in more detail, Marketing is a management responsibility and should not be solely left to junior members of staff. Marketing requires co-ordination, planning, implementation of campaigns and a competent manager(s) with the appropriate skills to ensure success.

Marketing objectives, goals and targets have to be monitored and met, competitor strategies analyzed, anticipated and exceeded. Through effective use of market and marketing research an organization should be able to identify the needs and wants of the customer and try to delivers benefits that will enhance or add to the customers lifestyle, while at the same time ensuring that the satisfaction of these needs resuits in a healthy turnover for the organization.

Within this exchange transaction customers will only exchange what they value (money) if they feel that their needs are being fully satisfied; clearly the greater the benefit provided the higher transactional value an organization can charge.

## 6.2 DEFINITION AND MEANING

The term marketing has changed and evolved over a period of time, today marketing is based around providing continual benefits to the customer, these benefits will be provided and a transactional exchange will take place.

Marketing has been viewed traditionally as a business activity. Business organizations exist to satisfy human needs, especially material needs. Consequently, one way to define marketing is from the business perspective. For instance, marketing has been defined as the "delivery of a higher standard of living."

**Important Point:** *"The management process responsible for identifying, anticipating and satisfying customer requirements profitably."* Chartered Institute of Marketing

*"Marketing as the performance of business activities that directs the flow of goods and services from producer to consumer or user".* American Marketing Association

*"Satisfying needs and wants through an exchange process".* Philip Kotler

*"A total system of business activities designed to plan, price, promote and distribute want satisfying goods and services to the present and potential customers".* William J. Stanton,

*"The management task of strategically planning, directing and controlling the application of enterprise effort to profit making programs which provide customer satisfaction - a task which involves the integration of all business activities into a unified system of action".*

Marting L. Bell's

The above definitions provide us an idea on the nature of marketing. The features in the above definitions are as follows:

(*a*) It is an exchange process.

(*b*) It covers a variety of functions to be carried out in an integrated manner.

(*c*) Marketing is directed to satisfy the needs/desires/wants of the consumer.

## 6.3 IMPORTANCE

Since marketing is consumer oriented, it has a positive impact on the business firms. It enables the entrepreneurs to improve the quality of their goods and services. Marketing helps in improving the standard of living of the people by offering a wide range of goods and services with freedom of choice, and by treating the customer as the most important and valuable person. The contribution of marketing in socio-economic system can be summarized as follows:

1. **National Income**: The nation's money is composed not of money, but of the goods and services which money can buy. Any increase in efficiency of the marketing process results in lower costs of distribution and lower prices to consumers. This brings an increase in the national income.
2. **Distribution Cost**: Marketing aims at reducing the cost of distribution to the extent possible to make it available to the consumers at reasonable price. It increases the consumption and profits of the firm. Hence, the shareholders may also get better share in profits. A part of the profit may also be utilized for further research work, for labour saving devices or for innovating new manufacturing techniques. Thus, the society is benefited in the long run.
3. **Production and Consumption**: Marketing process links the production and consumption. It brings new varieties, quality and beneficial goods to consumers from the manufacturing centers. A wealth of merchandise can be purchased at retail stores which were not available previously. It, thus, provides the connecting link between production and consumption and avoids the scarcity of goods.

4. **Business Slumps**: Scientific marketing has a stabilizing effect on the price level. Producers produce what consumers want and consumers have a wide choice of products, there are no frequent fluctuations in prices. A sound marketing system gives protection against business slump by discovering new markets, reducing cost of distribution, making it consumer oriented, diversifying and improving the product, extending after sales service etc.
5. **Transmutation**: The existence of a market and the specialists engaged in performing marketing functions are helpful in creating form utility to the hidden resources to suit the requirements of consumers. Thus, the consumer needs can be satisfied by the marketer.
6. **Productive Efficiency**: The information about the use of machinery and freely after sales services creates awareness of the latest development and helps in improving their productive efficiency.
7. **Imbalance in Supplies**: Scientific marketing remedies the imbalance in the supply by making available the surplus stocks at deficit areas. Through better provision of transport facilities and storage, market develops the trade in perishable goods, most of which at present go to waste.
8. **Value of Goods**: Place utility is created when a product is made readily accessible to the potential consumer. Time utility is created when a product is available to customers when they want it. Possession utility is created when a customer buys the product *i.e.*, the ownership title is transferred to the buyer.
9. **Value of Service**: Marketing adds value to the services *e.g.*, business, medical, entertainment and educational services by performing the services involved.
10. **Patterns of Consumption**: Patterns of consumption are determined by the structure of marketing system which is set up to carry the flow of goods and services from producer to consumers. The value added to the goods and services through performance of marketing activities also explains the pattern of consumption.
11. **Employment Opportunities**: Marketing is essential for full employment. There must be continuous marketing and high level of business activity to be continued. The continuous marketing activity is required for performing various marketing functions such as buying, selling, transportation, warehousing, financing, risk bearing, etc. Each function has countless job openings. It is a continuous source of employment and provides livelihood to a number of unemployed persons.
12. **Living Standards**: Marketing helps in increasing the standard of living of the people. It is logical that a reduction in the per unit cost of distribution of goods and services to the society would result in a higher standard of living.
13. **Expansion of Home Market**: Marketing can serve to expand the home market and thus provide a more secure base for export. When a country is self sufficient and is in a position to go for exports, it results in favourable balance of trade. It is an indicator of economic development of a country.

## 6.4 MARKETING ENVIRONMENT

The marketing environment surrounds and impacts upon the organization. There are three key elements to the marketing environment which are the internal environment, the micro-environment and the macro-environment. Why are they

important? Well marketers build both internal and external relationships. Marketers aim to deliver value to satisfied customers, so we need to assess and evaluate our internal business/corporate environment and our external environment which is subdivided into micro and macro.

**Important Point:** *"A company's marketing environment consists of the actors and forces outside marketing that affect marketing management's ability to build and maintain successful relationships with target customers."*

*"The marketing environment of the task environment and the broad environment. The task environment includes the immediate actors involved in purchasing, distributing and promoting the offering. The broad environment consists of six components: demographic environment, economic environment, natural environment, technological environment, political legal environment, social-cultural environment."*

### 6.4.1 Macro-Environment

It deals with the demographic, economic, technological, natural, socio-cultural and politico-legal environment of the markets. The following Fig. 6.1 shows the environmental framework.

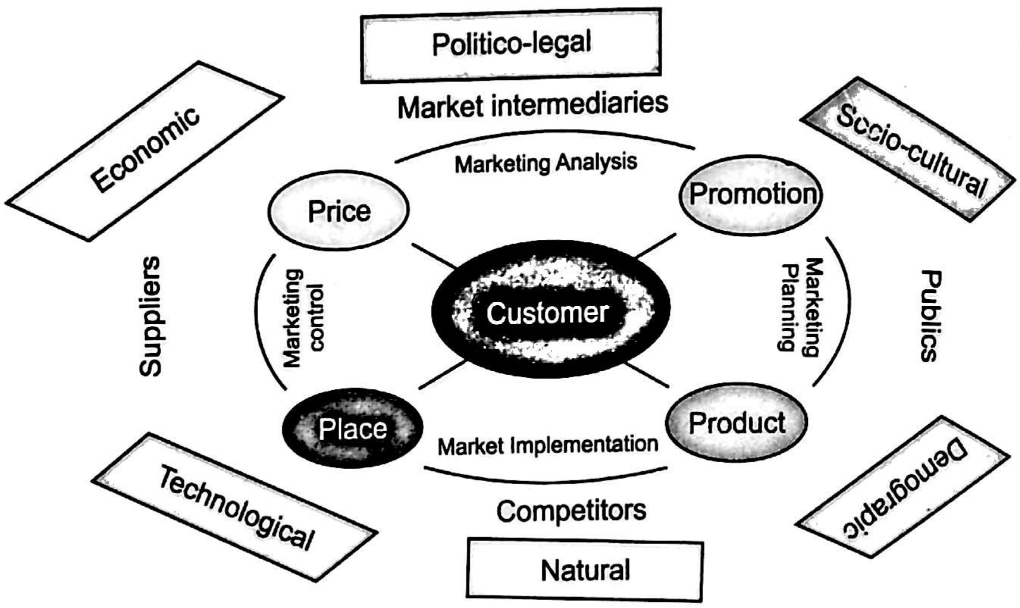


**Fig. 6.1** Environmental Framework

1. **Customers**: Customers are the core of the marketing environment. There are different types of customers such as end consumers, business customers, government customers, international customers and retailer customers.
2. **Suppliers**: A slightest delay in receiving the supplies may result in dissatisfaction of the customers. The marketers have to watch the supply availability and other trends related to the suppliers
3. **Marketing intermediaries**: The resellers, physical distribution firms, marketing services agencies, and financial intermediaries all make marketing intermediaries. They help in promotion of the company and sales and distribution of the company's products.

4. **Public:** Public is any group that has interest or impact on firm's ability to meet its goals. This includes the financial public, media public, government public, and local public such as NGO's and citizen action organizations.
5. **Competitors:** Competitors are the companies with similar offerings for goods and services. To remain competitive a company must consider who their biggest competitors are while considering its own size and position in the industry.
6. **Political-legal factors:** Political factors include how and to what degree a government intervenes in the economy. This includes monetary and tax policies of the government, labour laws, environmental laws, various trade restrictions, tariffs.
7. **Economic factors:** Economic factors are general economic growth, interest rates, exchange rates, balance of payments, monetary policies, inflation rate, etc. These factors play a very important role in business operations. These factors have the capability to alter the cost of operations, cost of capital and returns ultimately.
8. **Social factors:** Social factors are the social and cultural aspects, which include health consciousness, population growth rate, age distribution, career attitudes and emphasis on safety. They, have a major impact on demand of a firm's products and services.
9. **Technological factors:** Technological factors include the research and development, automation, expansion of internet and other communication technologies, technology incentives and technological barriers.
10. **Natural environment factors:** These factors include the weather, climate, and climate change, availability of water, availability of raw products, etc.

### 6.4.2 Micro-Environment

Marketing department let alone cannot satisfy all the needs of customer. Therefore it is essential to integrate the functions of suppliers, publics, company departments and intermediaries in creating the value to the customer. These forces are known as organization's micro environment. Micro-environment forces which are very close to company and have impact on value creation and customer service as shown in Fig. 6.2

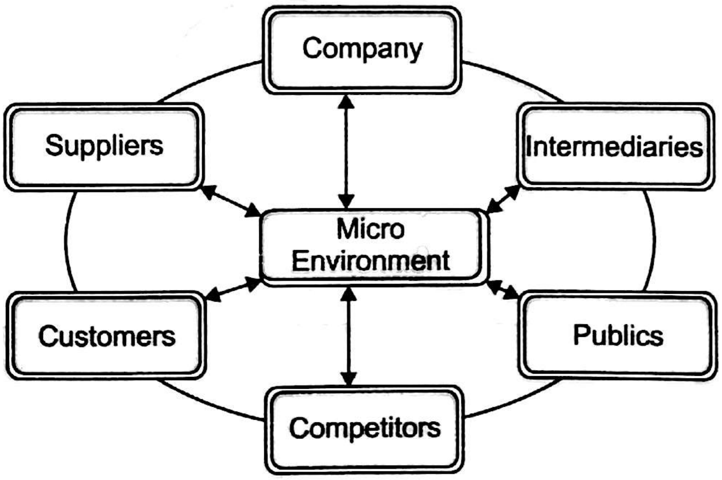


**Fig. 6.2** Micro-Environment

1. **The company:** Presuming a strategic plan in to specific marketing plan require coordination of other functions like finance, human resource, production, and research and development.
2. **Intermediaries:** The firms which distribute and sells the goods of the company to the consumer.
3. **Public:** These are micro-environment groups, which helps company to generate the financial resources, creating the image, examining the companies' policy and developing the attitude towards the product.
4. **Competitors:** A company should monitor its immediate competitor. The product should be positioned differently and able to provide better services.
5. **Suppliers:** Suppliers are the first link in the entire supply chain of the company. Hence any problems or cost escalation in this stage will have direct effect on the company. Many companies adopted supplier relation management system to manage them well.
6. **Customers:** A company may sell their products directly to the customer or use marketing intermediaries to reach them. Direct or indirect marketing depends on what type of markets the company serves.

## 6.5 SELLING

The terms 'marketing' and 'selling' are related but not synonymous. 'Marketing' as stated earlier, emphasizes on earning profits through customer satisfaction. In marketing, the focus is on the consumer's needs and their satisfaction. 'Selling' on the other hand focuses on product and emphasizes on selling what has been produced. In fact it is a small part of the wide process of marketing wherein emphasis is initially on promotion of goods and services and eventually on increase in sales volume.

Marketing has long term perspective of winning over consumer loyalty to the product by providing him maximum satisfaction. However, selling has short-term prospective of only increasing the sales volume.

In marketing, 'the consumer is the king', whose needs must be satisfied. In selling, the product is supreme and the entire focus is on sales volume. Marketing starts before production and continues even after the exchange of goods and services has taken place. It is so because provision of after sale service is an important component of marketing process. Selling starts after the production and ends as soon as the exchange of goods and services has taken place.

### 6.5.1 Difference between marketing and selling

| S.No. | Marketing | Selling |
|---|---|---|
| 1. | Marketing focuses on the needs of the buyer. | Selling focuses on the needs of the seller. |
| 2. | Converting customer's needs into product. | Converting product into cash. |
| 3. | Importance is given to the customer. | Importance is given to the product. |
| 4. | It focuses on customer satisfaction. | It focuses on sales volume. |
| 5. | It aims at long-term objective as it | It aims at short-term objectives, |

| | | |
|---|---|---|
| | has philosophical and strategic implications. | as it is only a tactical and routine activity. |
| 6. | Integrated approach to marketing is practiced. | Fragmented approach to selling is practiced. |
| 7. | It forecasts the customer needs to undertake the production activity. | It aims at selling the goods which are already produced through intensive promotion at a profit. |
| 8. | It gives top priority to profitable volume at fair and reasonable prices. | It gives priority to sales volume and maximization of profits through sales volume. |
| 9. | The principle of caveat vendor (*let the seller beware*) is followed. | The principle of caveat emptor (*let the buyer beware*) is followed. |
| 10. | Stresses on needs of buyer. | Stresses on needs of the seller. |

### 6.5.2 Selling concept

The selling concept in marketing is the notion that customers will not automatically buy something; they need to be sold it. This means that a persuasive advert or a sale assistant informing the customer that the product will change their life will make them buy something they most probably do not need or want.

According to the marketing website marketing91.com the consumers will not buy enough of the organization's products unless they are persuaded to do so through selling effort. So, organizations should undertake selling and promotion of their products for marketing success. The consumers typically are insert and they need to be forced for buying by converting their inert need in to a buying motive through persuasion and selling action.

### 6.5.3 Marketing concept

Marketing concept is the modern concept of marketing. Here the customer is considered as the soul of the entire marketing activity. The needs of customers are found out through marketing research and then products are developed to satisfy those needs. Building customer relationship and maintaining that relationship is given lot of importance. Customer is considered as the king of the market. This approach is used in today's globally competitive marketing world. The marketing concept rests on four pillars: target market, customer needs, integrated marketing and profitability.

### 6.5.4 Distinctions between the Marketing Concept and the Selling Concept:

| S.No. | Selling Concept | Marketing Concept |
|---|---|---|
| 1. | Focuses on the needs of the seller. | Focuses on the needs of the buyer. |
| 2. | Pre-occupied with the seller's need to convert his/her product into cash. | Pre-occupied with the idea of satisfying the needs of the customer by means of the product as a solution to the customer's problem (needs). |

## 6.6 SOCIETAL MARKETING CONCEPTS

The marketing concept has evolved into a fifth and more refined company orientation: The societal marketing concept. This concept is more theoretical and will undoubtedly influence future forms of marketing and selling approaches.

Societal marketing is basically a marketing concept that is of the view that a company must make good marketing decisions after considering consumer wants, the requirements of the company and most of all the long term interests of the society.

Societal marketing is actually a subsidiary of the concept of corporate social responsibility and sustainable development. This concept urges companies to do more than having an exchange relationship with customers, to go beyond delivering products and work for the benefit of the consumers and the society.

Following are the three examples of societal marketing concept:

1. **Body Shop**: Body shop is a cosmetic company found by Anita Roddick. The company uses only vegetable based materials for its products. It is also against animal testing, supports community trade, activate self esteem, defend human rights, and overall protection of the planet. Thus it is completely following the concept of Societal Marketing.
2. **Ariel**: **Ariel** is a detergent manufactured by Procter and Gamble. Ariel runs special fund raising campaigns for deprived classes of the world specifically the developing countries. It also contributes part of its profits from every bag sold to the development of the society.
3. **British American tobacco Company**: BAT is a British based Tobacco company. It was found in the year 1902. BAT is involved in working for the society in every part of the world. It conducts tree plantation drives as part of its societal marketing strategy.

## 6.7 MARKETING MIX: 4 P'S,

The marketing mix is one of the most famous marketing terms. The marketing mix is the tactical or operational part of a marketing plan. The marketing mix is also called the 4P's and the 7P's. The 4P's are price, place, product and promotion. The services marketing mix is also called the 7P's and includes the addition of process, people and physical evidence.

**Important Point**: *"Marketing Mix is the set of controllable variables that the firm can use to influence the buyer's response".*

*Philip Kotler*

The controllable variables in this context refer to the 4'P's [product, price, place (distribution channel) and promotion]. Each firm strives to build up such a composition of 4'P's, which can create highest level of consumer satisfaction and at the same time meet its organizational objectives. Thus, this mix is assembled keeping in mind the needs of target customers, and it varies from one organization to another depending upon its available resources and marketing objectives.

Let us now have a brief idea about the four components of marketing mix. The Fig. 6.3 displays the component of mixing.

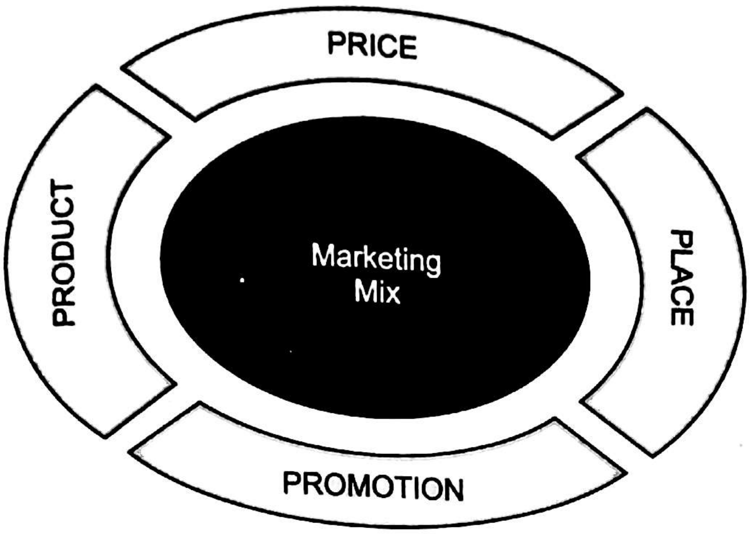


**Fig. 6.3 Component of Marketing Mix: The 4 P's**

1. **Product**: Product refers to a physical product or a service or an idea which a consumer needs and for which he is ready to pay. Physical products include tangible goods like grocery items, garments, footwares, etc. Services are intangible products which are offered and purchased by consumers. Services may involve also an innovative idea on any aspect of operation. Products are the key element of any marketing mix. The decisions concerning product may relate to:
   (*a*) Product attributes,
   (*b*) Branding,
   (*c*) Packaging and labeling,
   (*d*) Product support service,
   (*e*) Product mix.
2. **Price**: Price is the amount charged for a product or service. It is the second most important element in the marketing mix. Fixing the price of the product is a complicated job. Many factors like demand for a product, cost involved, consumer's ability to pay, prices charged by competitors for similar products or prevailing prices, government restrictions, etc. have to be kept in mind while fixing the price. In fact, pricing is a very crucial decision area as it has its effect on demand for the product and also on the profitability of the firm.
3. **Promotion**: If the product is manufactured keeping the consumer needs in mind, is rightly priced and made available at outlets convenient to them. But if the consumer is not made aware about its price, features, availability etc., its marketing effort may not be successful. Therefore promotion is an important ingredient of marketing mix as it refers to a process of informing, persuading and influencing a consumer to make choice of the product to be bought. Promotion is done through means of personal selling, advertising, publicity and sales promotion. It is done mainly with a view to provide information to prospective consumers about the availability, characteristics and uses of a product. It arouses potential consumer's interest in the product, compare it with competitors' product and make his choice. The proliferation of print and electronic media has immensely helped the process of promotion.

4. **Place**: Goods are produced to be sold to the consumers. They must be made available to the consumers at a place where they can conveniently make purchase. Woolens are manufactured on a large scale in Ludhiana and you purchase them at a store from the nearby market in your town. So, it is necessary that the product is available at shops in your town. This involves a chain of individuals and institutions like distributors, wholesalers and retailers who constitute firm's distribution network (also called a channel of distribution). The organization has to decide whether to sell directly to the retailer or through the distributors/wholesaler, etc. It can even plan to sell it directly to consumers.

## 6.8 CONSUMERS

Consumers are individuals, households or businesses who use the products. Most products eventually end up in private households even though they will pass through a number of steps on their way from producer to end user. Producers and traders form vertical chains or networks, called value chains, at the end of which are the consumer. Understanding consumer behaviour is not only important for the producer but for all the other players in the chain. The value that the consumer puts on the goods or services limits what everyone else can get from the value chain.

### 6.8.1 Characteristics of Consumer Behaviour

Consumer behaviour attempts to understand the buyer decision making process, both individually and in groups. It studies characteristics of individual consumers such as demographics and behavioural variables in an attempt to understand what people's wants. It also tries to assess influences on the consumer from groups such as family, friends, reference groups and society in general. The various variables attempts to influence on consumers are as follows:

1. **Demographics Variables**: These are current statistical characteristics of a population. These types of data are used widely in sociology, public policy, and marketing. Commonly examined demographics include gender, race, age, disabilities, mobility, home ownership, marital status, employment status, and even location. Demographic trends describe the historical changes in demographics in a population over time for example, the average age of a population may increase or decrease over time. Both distributions and trends of values within a demographic variable are of interest. Demographics are about the population of a region and the culture of the people there.
2. **Behavioural Variables**: The behavioural variable of market segmentation group's consumers in terms of occasions, usage, loyalty and benefits sought. This is based on the way different consumers respond to, use or know a product or service. The variable of occasion simply means the occasion on which a product or service is consumed or purchased. The behavioural variable includes:
   (i) **Attitudes**: It represents what consumer like and dislike. An attitude is a lasting general evaluation of something-it has knowledge of that something, liking or disliking, and the strength of the feelings. They

are lasting, but changeable. They help to direct behaviour – *e.g.* do you recycle cans?

(ii) **Motivation**: People are motivated by many things, some positive others not. Some motivating factors can move people only a short time, like hunger which will last only until you are fed. Others can drive a person onward for years. Motivation is the driving force within individuals that forces them to action. Motivation is the activation or energisation of goal-oriented behaviour.

(iii) **Perceptions**: Perception can be described as "how we see the world around us". All the time we are receiving messages through our five organs viz., eyes, ears, nose, mouth and skin. The different sights, sounds, smells, tastes and sensations that we feel are knows as stimuli.

(iv) **Personality**: The term personality is sum total of an individual's psychological traits, characteristics, motives, habits, attitudes, beliefs and outlooks. Personality is the very essence of individual differences. In consumer behaviour, personality is defined as those inner psychological characteristics that both determine and reflect how person responds to his environmental stimuli. Personality is enduring and ensures that a person's responses are consistent over time.

Personality research to predict consumer behaviour has either focused on total personality profile or a specific trait or attempted to find a correlation with product brand choice. But both these approaches assume that individuals with a given personality profile or trait are homogeneous in all other respects such as age, income, education, occupation, etc.

(v) **Lifestyle**: A consumer's lifestyle bears the influence of his participation in social groups and of his relationships with others. An individual's lifestyle may result in certain consistency of behaviour. Knowing a person's conduct in one aspect of life may enable us to predict how he/she may behave in other areas.

(vi) **Knowledge**: The success or failure of products and services is ultimately determined by their acceptance in consumer markets. The consumer behaviour knowledge domain seeks to understand the psychology and behaviour of consumers—particularly consumer attitudes and buying behaviour.

### 6.8.2 COGNITIVE DISSONANCE

In 1956, **Leon Festinger** coined the term 'Cognitive Dissonance'. Cognitive dissonance is a discomfort caused by holding conflicting cognitions (*e.g.*, ideas, beliefs, values, emotional reactions) simultaneously. In a state of dissonance, people may feel surprise, guilt, anger, or embarrassment. In a theory of cognitive dissonance, the concept can be defined as:

**Important Point**: *"The psychological opposition of irreconcilable ideas (cognitions) held simultaneously by one individual, created a motivated force that would lead, under proper conditions, to the adjustment of one's belief to fit one's behaviour – instead of changing one's behaviour to fit one's belief (the sequence conventionally assumed)".*

The theory of cognitive dissonance in social psychology proposes that people have a motivational drive to reduce dissonance by altering existing cognitions, adding new ones to create a consistent belief system, or alternatively by reducing the importance of any one of the dissonant elements. An example of this would be the conflict between wanting to smoke and knowing that smoking is unhealthy; a person may try to change their feelings about the odds that they will actually suffer the consequences, or they might add the consonant element that the smoking is worth short term benefits. A general view of cognitive dissonance is when one is biased towards a certain decision even though other factors favour an alternative.

## 6.9 BUSINESS AND INDUSTRIAL MARKET

One observes that the role of marketing in modern organization is that of integrating the needs and wants of the customers to the other organizational functions like production, R&D, finance, personnel, etc. One look at the companies today would be sufficient to conclude that neither marketing nor any other function alone holds the key to success. All functions are equally important. However it is marketing, which performs the role of integration.

1. **Corporate Marketing:** Provide information on competition, customer and advocate customer orientation for developing long-term corporate strategy.
2. **Strategic Marketing:** Provide competition and customer analysis for developing long-term business strategy, including competitive advantage. Develop segmenting, targeting and positioning strategies and take product line decisions.
3. **Marketing Management:** Evolve and implement marketing strategy in short term to achieve business unit objectives. Coordinate marketing activities and allocate resources.

## 6.10 MARKET TARGETING

Target marketing refers to a concept in marketing which helps the marketers to divide the market into small units comprising of like minded people. Such segmentation helps the marketers to design specific strategies and techniques to promote a product amongst its target market. A target market refers to a group of individuals who are inclined towards similar products and respond to similar marketing techniques and promotional schemes.

**Important Point:** *"Market targeting is made up of evaluation of market segment and selection of market segment/segments to be in".*

### 6.10.1 Targeting Strategies

Once a firm has identified the market segments it wishes to target, it needs to develop effective targeting strategies for these segments. Targeting strategies tend to follow certain methods to maximize their effectiveness. These are as following:

1. **Single segment strategy:** A single segment strategy involves the firm choosing its single preferred market segment and targeting it with a single marketing

mix, aimed at serving the segment as much as possible. This is generally chosen by a smaller firm, or one which has only located one attractive market segment.

2. **Selective specialization**: This is a multiple-segment strategy, also known as a differentiated strategy. Different marketing mixes are offered to different segments. The product itself may or may not be different-in many cases only the promotional message or distribution channels vary.
3. **Product specialization strategy**: A product specialization strategy occurs when a firm possesses a particularly attractive product, and hence tailors it to a variety of feasible market segments.
4. **Market specialization strategy**: A market specialization strategy involves a firm which finds one market segment very attractive, and hence that segment a variety of different products. This is often done by a firm to fill up a segment, and hence discourage any competitors from entering.
5. **Full market coverage**: It occurs when a firm tries to serve all segments in an entire market. This does not always imply a mass market strategy; instead a firm can offer a variety of marketing mixes to every major segment in a market. This is what many supermarket chains have attempted with their value, standard and premium ranges.

The following diagrams 6.4 show examples of the five market selection patterns given three market segments $S_1$, $S_2$, and $S_3$, and three products $P_1$, $P_2$, and $P_3$.

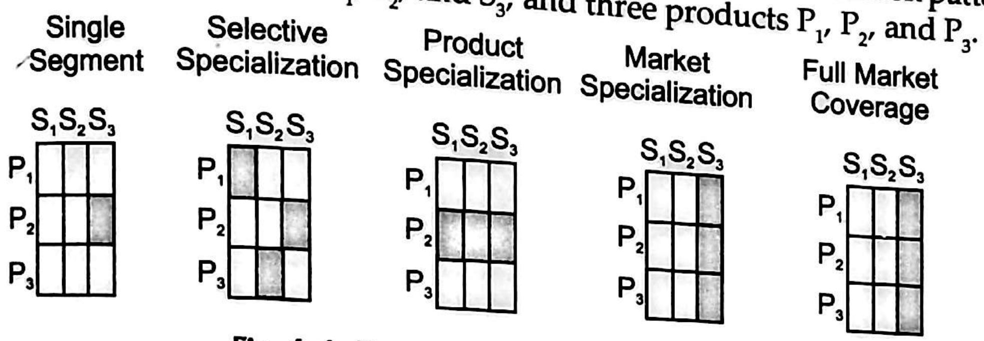


**Fig. 6.4** Five market selection patterns

A firm that is seeking to enter a market and grow should first target the most attractive segment that matches its capabilities. Once it gains a foothold, it can expand by pursuing a product specialization strategy, tailoring the product for different segments, or by pursuing a market specialization strategy and offering new products to its existing market segment.

Another strategy whose use is increasing is individual marketing, in which the marketing mix is tailored on an individual consumer basis. While in the past impractical, individual marketing is becoming more viable thanks to advances in technology.

## 6.11 POSITIONING

Positioning follows on logically from the segmentation and targeting stages. Customer perceptions are central to the product position especially in relation to the competition's offering. The product or service has to satisfy key customer requirements and this has to be clearly communicated to customers.

Positioning is the last stage in the Segmentation Targeting Positioning Cycle. Once the organization decides on its target market, it strives hard to create an

image of its product in the minds of the consumers. The marketers create a first impression of the product in the minds of consumers through positioning.

**Important Point:** *"The process of creating an image of a product in the minds of the consumers is called as positioning. Positioning helps to create first impression of brands in the minds of target audience".*

In simpler words positioning helps in creating a perception of a product or service amongst the consumers. Example: The brand "Bisleri" stands for purity and the brand "Ceat Tyre" stands for better grip.

As the companies increase the number of claims for their brand, they risk disbelief and a loss of clear positioning. In general, a company must avoid four major positioning errors.

1. **Under positioning:** Some companies discover that buyers have only a vague idea of the brand. The brand is seen as just another entry in a crowded marketplace.
2. **Over- positioning:** Buyers may have too narrow image of the brand.
3. **Confused Positioning:** Buyers might have a confused image of the brand resulting from the company's making too many claims or changing the brand's positioning too frequently.
4. **Doubtful Positioning:** Buyers may find it hard to believe the brand claims in view of the product's features, price or manufacturer.

### 6.11.1 Steps to Product Positioning

Marketers with the positioning process try to create a unique identity of a product amongst the customers.

1. **Know your target audience well:** It is important to identify the target audience and then understand their needs and preferences. The products must fulfill the demands of the individuals. Every individual has different interests, needs and preferences. No two individuals can think on the same lines.
2. **Identify the product features:** The marketers themselves must be well aware of the features and benefits of the products. A marketer selling Samsung phones should himself also use a Samsung handset for the customers to believe him.
3. **Unique selling Propositions:** The marketers must themselves know what best their product can do. Every product should have Unique Selling Propositions at least some features which are unique. Find out how the products can be useful to the end-users? For Example why do people use "Anti Dandruff Shampoo?"

   Anti Dandruff Shampoos are meant to get rid of dandruff. This is how the product is positioned in the minds of the individuals. Unique Selling Propositions USP of a Nokia Handset - Better battery backup.
4. **Know your competitors:** A marketer must be aware of the competitor's offerings. Let the individuals know how your product is better than the competitors? Let the target audience know how your product is better than others.
5. **Never compromise on quality:** Do not drastically reduce the price of your

products. A Rado watch would lose its charm if its price is equal to a Sonata or a Maxima Watch.

## 6.12 ADVERTISING

Advertising is non-personal as it is not directed to any single individual. Secondly, the sponsor *i.e.*, the manufacturer or producer is identified as his name and address is always contained in an advertisement and he also bears all the cost involved in the process. Thirdly, the producer can also promote an idea regarding quality, design, packing and pricing, etc. of any product or service.

*"Advertising is any form of paid non-personal presentation of ideas, goods or services for the purpose of inducting people to buy".*

*According to Wheeler*

*"Advertising is a paid form of non-personal presentation of ideas, goods or services by an identified sponsor".*

*Richard Buskirk*

*"Advertising consists of all the activities involves in presenting to a group, a non-personal, oral or visual, openly sponsored message regarding disseminated through one or more media and is paid for by an identified sponsor".*

### 6.12.1 The 5- M's of Advertising

In developing a program, marketing managers must always start by identifying the target market and the buyer's motives. Then they can make the five major decisions in developing an advertising program, known as the 5- M's, viz.

**Mission**: what are the advertising objectives?

**Money**: how much can be spent?

**Message**: what message can be sent?

**Media**: what media should be used?

**Measurement**: how should the results is evaluated? The above mentioned can be explained by the Table 6.1 given below:

**The 5Ms of Advertising**

Checklist for planning of a marketing or advertising campaign.

**Table 6.1 Five M's of Advertising**

| | |
|---|---|
| **Mission** | What are the objectives?<br>What is the key objective? |
| **Money** | How much is it worth to reach my objectives?<br>How much can be spent? |
| **Message** | What message should be sent?<br>Is the message clear and easily understood? |
| **Media** | What media vehicles are available?<br>What media vehicles should be used? |
| **Measurement** | How should the results be measured?<br>How should the results be evaluated and followed up? |

### 6.12.2 Advertising Budgeting Methods

There is several allocation methods used in developing an advertising budget. The most common are listed below:

1. Percentage of sales method
2. Objective and task method
3. Competitive parity method
4. Market share method
5. Unit sales method
6. All available Funds method
7. Affordable method

It is important to notice that most of these methods are often combined in any number of ways, depending on the situation. Because of this, these methods should not be seen as rigid, but rather as building blocks that can be combined, modified, or discarded as necessary. Remember, a business must be flexible—ready to change course, goals, and philosophy when the market and the consumer demand such a change.

## 6.13 PUBLICITY

Publicity is one component of promotion which is non-personal stimulation of demand for a product, service or business unit by placing commercially significant news about it in a published medium or obtaining favourable presentation of it upon radio, television, or stage that is not paid for by the sponsor. The crucial aspect of publicity is that it should emanate from a neutral and impartial source such as editorial material and is not paid for by the sponsor. To achieve the aim of credibility it should not raise any doubts regarding interested sponsorship. Publicity and public relations have a lot in common. In fact, publicity is one of the tools of public relations.

The advantages of publicity are low cost, and credibility particularly if the publicity is aired in between news stories like on evening TV news casts. New technologies such as web-blogs, web cameras, web affiliates, and convergence (phone-camera posting of pictures and videos to websites) are changing the cost-structure. The disadvantages are lack of control over how your releases will be used, and frustration over the low percentage of releases that are taken up by the media.

### 6.13.1 Difference Between Advertisement And Publicity

The difference between advertisement and publicity is as following:

| S. no. | Advertisement | Publicity |
|---|---|---|
| 1. | Advertising is the process of letting the public knows of the new product or service or of any alterations to the existing one with the main aim of offering it for sale | Publicity is informing the world about news events or ground breaking developments in the company through radio, television, magazines, pamphlets, or |

| | | |
|---|---|---|
| | to gain profit. Advertising can be done through all sorts of media. | newspapers. The publicity is usually picked up by news or industry related media and is not a paid advertisement. |
| 2. | The advertisement is paid form of communication. | Whereas publicity is not a paid form of communication. |
| 3. | In advertisement, company purchases some space in Newspaper, Magazines to aware the customer about his latest launched product. | But publicity is free of cost and it is non-personal communication of information that is not paid for by an individual or organization. |
| 4. | Advertisement is issued by an identified sponsor. | Whereas in publicity sponsor is not identified. |
| 5. | Advertising is controllable by the organization/sponsor. | While publicity is not controllable because it comes from an unbiased source. |
| 6. | Most of the times in advertising social responsibility are ignored. | While in publicity special focus is given on social responsibility. |
| 7. | In advertising, the advertisers get to fully exercise their creativity as they create new materials and ad campaigns. | Publicity is limited to how you look for any new information that you can give the media. |
| 8. | Advertisements are aired to create positive image among customers. | Publicity may create positive or negative image. |
| 9. | Since you pay for the space, you can run your ads over and over for as long as your budget allows. An ad generally has a longer shelf life than one press release. Sponsor has full awareness about the timing and location of ad appearance. | Whereas in publicity, any coverage usually runs only once, and firm do not know when and where the coverage will appear. |

### 6.13.2 Publicity Techniques

The following sections list numerous means by which you can publicize events.

1. **Posters:** The essential purpose of a poster is the rapid telling of a single simple message using a limited number of elements. Posters are viewed more rapidly than other methods of advertisement. Their message must be strong, simple, and brief.
2. **Invitations:** A personal touch can be added to your publicity by distributing invitations for your program. These can be placed in mailboxes or handed out or slipped under room doors.

3. **Calendars:** A large calendar of activities located on your bulletin board or distributed individually is a particularly effective technique. Students will have at least one consistently identifiable source for information and activities. The smaller calendars of activities can be copied and put into mailboxes or slide under doors.
4. **Balloons:** We can write a message on the balloon or put the message on a piece paper inside the balloon. Balloons can be tied with string to door knobs, handed out at the entrance of the building or handed out in dining hall lines.
5. **Tickets:** We can purchase printed tickets or make your own. Free tickets, and Invitations, can be placed in mailboxes, handed out, or slipped under doors. A variation of the ticket concept is to distribute coupons. The coupon might entitle the person to a prize or free refreshment item. Coupons can be included on flyers or on printed schedules and this may prevent your advertisement from falling victim to the trash can.
6. **Banners:** A large extension of the poster, these can be hung outside the hall or in the mailroom or in a lobby. A bed sheet or old shower curtain will make a good size banner.
7. **Word of Mouth:** And of course, there is the time-honored word-of-mouth technique. This is perhaps the oldest, yet most effective way to get the word out. Its effectiveness should not be underestimated. Go door to door and personally inform people of the activity; and remind them frequently, so that they do not forget.

## 6.14 CRM (CUSTOMER RELATIONSHIP MANAGEMENT)

In IT terms, "CRM means an enterprise-wide integration of technologies working together such as Data warehouse, website, Intranet/extranet, phone support system, marketing, production, R etc. CRM has many similarities with Enterprise Resource Planning (ERP), where ERP can be considered back-office integration and CRM as front-office integration. A notable difference between ERP and CRM is that, ERP can be implemented without CRM. However, CRM usually requires access to the back-office data that often happen through ERP-type integration.

**Important Point:** *"CRM is a business strategy with outcomes that optimize profitability, revenue and customer satisfaction by organizing around customer segmentation, fostering customer satisfying behaviours and implementing customer centric processes. CRM technologies should enable greater customer insight, increases customer access, more effective interactions and integration's throughout all customer channel and back office enterprise functions".*

CRM principally revolves around marketing and begins with a deep analysis of consumer behaviour. It uses IT to gather data, which can be used to develop information required to create a more personal interaction with the customer. In long term, it produces a method of continuous analysis and refinement in order to enhance customers lifetime value (CLV) with firm. Well et. al. (1999) noted, "Both (marketing & IT) need to work together with a high level of co-ordination to produce a seamless process of interaction". However, in order to work effectively with marketing, IT managers need an understanding of the fundamental marketing motivation driving the CRM trend.

## 6.14.1 Types of CRM

CRM allows a company to address all of the types of customers it serves at different points in their life cycle and to choose the marketing program that best fits a customer's attitude toward the company and willingness to purchase its products and services. There are 4-types of CRM:

1. **Win-Back or Save**: This is the process of convincing a customer to stay with the organization at the point they are discontinuing service or convincing them to rejoin once they have left.

   Of the four categories of campaigns, win-back is the most sensitive. Research indicates that win-back campaign is 4-times more likely to succeed if contact is made within the first week following a defection than if it is made in the fourth week. Selectivity is the other essential characteristics of a successful win-back campaign.

2. **Prospecting**: Prospecting is the effort to win new, first time customers. Apart from the offer itself; the three most critical elements of a prospecting campaign are segmentation, selectivity and source. It is essential to develop an effective needs based segmentation model that allows the organization to effectively target the offer. Without this focused approach, the organization either fails to achieve an adequate acceptance or rate an the offer or spends too much on promotions, advertising and concessionary pricing. It is advisable to achieve a 95% confidence rate before embarking on a prospecting effort.

   Selectivity is as important to prospecting as it is to win-back. Needs-based segmentation defines what the customer wants from the organization and the profit based segmentation, define how valuable the customer is and helps the organization to decide how much it is willing to spend to get that customer. Pre-scoring a customer credit rating is one of the techniques that organization can use to determine the later.

3. **Loyalty**: Loyalty is the category in which it is most difficult to gain accurate measures. The organization is trying to prevent customers from leaving and uses three essential elements as shown in Fig. 6.5.

   ⇒ Value-Based segmentation;

   ⇒ Need-Based segmentation

   ⇒ Predictive Churn Models.

   **Value-Based segmentation**–It allows the organization to determine how much it is willing to invest in retaining a customer's loyalty.

   **Needs-Based segmentation**–Once the customer has passed the value based segmentation, the organization can use needs-based segmentation to offer a customized loyalty program.

   **Predictive Churn Models**–Using the vast amount of demographic data and usage rate available for the existing base of customers which helps in forecasting customer attrition. Through the use of advanced data-mining tools, organization can develop models that identify vulnerable and potential customer's which can be targeted for the loyalty campaign or offered alternative products.

4. **Cross-Sell/Up-sell:** The purpose is to identifying complementary offering that a customer would like. For example: a basic long distance customer could be a candidate to buy Internet access.

   Customer's need-based segment, usage pattern and reaction to previous contacts/interactions determine the nature of the offer. Once the composition of the offer is determined and the contact medium is agreed to, presents that offer to the customer.

   Up selling is similar, but instead of offering a complementary product, the organization offers an enhanced one.

   For example: Replacing an analog data line with ISDN.

   Cross sell/Up-sell campaigns are important because the customer targeted already have a relationship with the organization. They are less likely to see the offer as a commodity and are thus more willing to pay a premium for it. In financial terms, when customer accepts a cross-sell or up-sell offer, that customer begins to become much more profitable.

### 6.14.2 Implementing CRM with Critical Success Factors

Critical success factors (CSFs) have been used significantly to present or identify a few key factors that organizations should focus on to be successful. As a definition, critical success factors refer to "the limited number of areas in which satisfactory results will ensure successful competitive performance for the individual, department, reorganization" as shown in Fig. 6.5 Identifying CSFs is important as it allows firms to focus their efforts on building their capabilities to meet the CSFs, or even allow firms to decide if they have the capability to build the requirements necessary to meet critical success factors (CSFs).

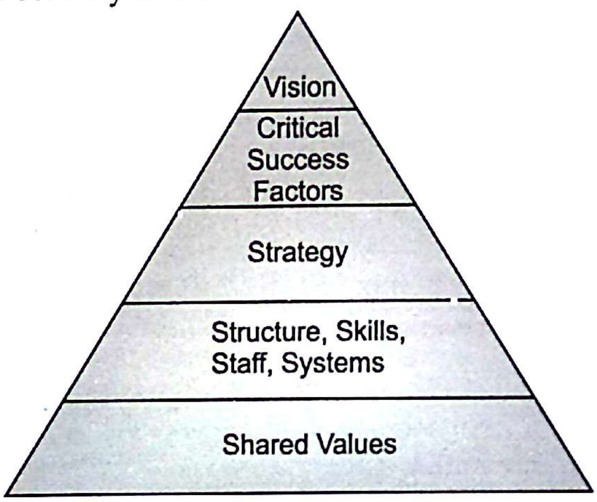


**Fig. 6.5** Critical Success Factors (CSF)

Critical success factors are the areas of your business or project that are absolutely essential to its success. By identifying and communicating these CSFs, you can help ensure your business or project is well-focused and avoids wasting effort and resources on less important areas. By making CSFs explicit, and communicating them with everyone involved, you can help keep the business and project on track towards common aims and goals. "Identifying your CSFs is a very iterative process. Your mission, strategic goals and CSFs are intrinsically

linked and each will be refined as you develop them. Here are the summary steps that, used iteratively, will help you identify the CSFs for your business or project:

**Step One:** Establish your businesses or project's mission and strategic goals.

**Step Two:** For each strategic goal, ask yourself "what area of business or project activity is essential to achieve this goal?" The answers to the question are your candidate CSFs.

**Step Three:** Evaluate the list of candidate CSFs to find the absolute essential elements for achieving success - these are your Critical Success Factors. As you identify and evaluate candidate CSFs, you may uncover some new strategic objectives or more detailed objectives. So you may need to define your mission, objectives and CSFs iteratively.

**Step Four:** Identify how you will monitor and measure each of the CSFs.'

**Step Five:** Communicate your CSFs along with the other important elements of your business or project's strategy.

## 6.15 MARKET RESEARCH

**Marketing Research** has two words, viz., "Marketing" and "Research".

(i) **Marketing** means buying and selling activities with consumer satisfaction.

(ii) **Research** means a systematic and complete study of a problem. It is done by experts. It uses scientific methods. Thus, we can say, Marketing Research is a systematic method of collecting, recording and analyzing of data which is used to solve marketing problems.

Marketing Research (MR) may be defined as systematic collection and analysis of data relating to the marketing of goods and services. Different scholars have defined it in different ways.

> **Important Point:** *"Systematic problem analysis, model building and fact finding for the purpose of important, decision making and control in the marketing of goods and services".*
>
> *"Marketing Research is the function that links the consumer, customer and public to the marketer through information used to identify and define marketing opportunities and problems, generate, refine and evaluate marketing actions; monitor marketing performance; and improve understanding of marketing as a process."* — *American Marketing Association*

### 6.15.1 Market Research vs Marketing Research

**Market Research:** Researching is the immediate competitive environment of the market place, including customers, competitors, suppliers, distributors and retailers.

**Marketing Research:** Includes the entire above plus:

- Companies and their strategies for products and markets,
- The wider environment within which the firm operates (*e.g.* political, social, etc).

### 6.15.2 The Marketing Research Process

For marketing research to be systematic, it has to follow a number of steps. This following Fig. 6.6 showed the different step of marketing research.

**1. Defining the Problem:**

**Important Point:** *"A problem well defined is a problem half-solved."* – *John Dewey.*

First, the purpose of the research needs to be established. This can be done by specifying what marketing decisions need to be made and what marketing problems are to be addressed, using information from the marketing research project.

2. **Research Objective:** Next the research objectives have to be established: exactly which questions are to be answered by the research? Research objectives may be state in qualitative or quantitative terms and expressed as research question statements or hypothesis. For example, the research objective "To find out the extent to which the sales promotion programs affected sales" is a research objective expressed as a statement.

Defining the Problem
↓
Statement of Research Objectives
↓
Planning a Research Design
↓
Planning a Sample
↓
Collecting the Data
↓
Analysing the Data
↓
Formulating Conclusion
↓
Preparing & Presenting the Report

**Fig. 6.6** Steps for Marketing Research Process

3. **Planning the Research Design:** Once the research problem has been defined and the objectives decided, the research design must be developed. A research design is a plan specifying the procedure for collecting and analyzing the needed information. It represents framework for the research plan of action.
4. **Planning the Sample:** Although the sample plan is included in the research design. The actual sampling is a separate and important stage in the research process. Sampling involves procedures that use a small number of items or parts of the population to make conclusion regarding the whole population.
5. **Data Collection:** The researcher will need to ensure that the study will be relevant to the problem and will use economical procedures. The data

collection process follows the formulation of research design including the sampling plan. Data which can be secondary or primary can be collected using variety of tools. Some methods of data collection are as following:

(i) **Focus Groups**: This is excellent approach to gather in-depth attitudes, beliefs, and anecdotal data from a large group of patrons at one time. Group dynamics might generate more ideas than individual interviews. They can be effectively used to focus on details regarding issues found through surveys or other data collection methods. Participants are not required to read or write. Technique relies on oral communication.

(ii) **Interviews**: It is good approach to gather in-depth attitudes, beliefs, and anecdotal data from individual patrons. Personal contact with participants might elicit richer and more detailed responses. It provides an excellent opportunity to probe and explore questions. It participants do not need to be able to read and write to respond.

(iii) **Observation**: It is excellent approach to discover behaviours. It provides indicators of the impact of programs that might be more reliable than data gained by asking people.

(iv) **Surveys**: Best for gathering brief written responses on attitudes, beliefs regarding library programs. They can include both close-ended and open-ended questions. They can be administered in written form or online. Personal contact with the participants is not required. Staff and facilities requirements are minimal, since one employee can easily manage the distribution and collection of surveys, and issues such as privacy, quiet areas, etc. are typically not concerns.

6. **Data Processing and Analysis**: Once the data has been collected, it needs to be processed and analyzed. The processing involves converting the raw data, by 'coding', into a form which can be analyzed. Coding is a process whereby categories for responses are established, so that numbers can be used to represent the categories. The final stages involve the analysis of data and the presentation of the results to management. The analysis needs to be undertaken so as to answer the questions originally posed.

7. **Formulating Conclusion**: The next stage in the research process is that of interpreting the information and drawing conclusions for use in managerial decisions.

8. **Preparing and Presenting the Report**: This is the final stage of research process. Often the management is not interested in details of research design and statistical analysis but in the concrete findings of the research. Researchers, therefore, must make the presentation technically accurate, understandable and useful. Frequently, the researchers are required to make both an oral and a written presentation.

## REVIEW QUESTIONS

1. What is marketing? Explain the meaning and importance of marketing.
2. Bring out the difference between macro environment and micro environment.
3. Discuss the importance of political and legal environment study with examples.
4. Differentiate between need, want and demand. *(R.G.P.V., Dec. 2009)*
5. What a demand-supply forces and their effect on cost? *(R.G.P.V., June 2010)*

6. What is the importance of relationship in marketing? (R.G.P.V., Dec. 20
7. Explain four P's of marketing-product, price, placement and promotion. (R.G.P.V., Dec. 20
8. What is difference between marketing and selling?
9. What do you meant by consumer behaviour? Explain the characteristics of consumer behavio
10. Define market targeting and targeting strategies.
11. What is advertising? Explain the 5- M's of advertising.
12. Explain the advertising budgeting methods.
13. What is publicity? Explain the difference between advertisement and publicity.
14. What is CRM? Explain different types of CRM. (R.G.P.V., June. 2010, Dec. 201
15. What is Meaning and concepts of positioning?
16. Explain the different steps to product positioning.
17. What is market research? Explain the marketing research process.

# 7 Finance Management

## Chapter Outline

- Introduction
- Meaning and Definition
- Features of Finance Management
- Nature and Scope
- Forms of Business Ownerships
- Balance Sheet
- Profit and Loss Account (P & L A/C)
- Working Capital Management
- Fund Flow and Cash Flow Statements
- Break Even Point (BEP)
- Financial Ratio Analysis
- Capital Budgeting
  - ⇒ Payback Period
  - ⇒ Net Present Value (NPV)
  - ⇒ Internal Rate of Return (IRR)

## 7.1 INTRODUCTION

Finance is the blood of the business. Without finance neither any business can be started nor successfully run. Finance is needed to promote or establish any business, acquire fixed assets, make necessary, investigations, develop product keep man and machines at work, encourage management to make progress and create values.

Financial management in the firm is characterized in many different cases by the need to face up to a somewhat different set of problems and opportunities than those confronted by a large corporation. One immediate and obvious difference is that a majority of smaller firms do not normally have the opportunity to publicly sale of stocks or bonds in order to raise funds. The owner of a firm must reply primarily on trade credit, bank financing, lease financing, and personal equity to finance the business. One therefore faces a much more severely restricted set of financing alternatives than those faced by the financial vice president or treasurer of a large corporation.

## 7.2 MEANING AND DEFINITION OF FINANCE MANAGEMENT

Financial management entails planning for the future for a person or a business enterprise to ensure a positive flow of cash. It includes the administration and maintenance of financial assets. Besides, financial management also covers the process of identifying and managing risk.

**Important Point:** *"Financial management is concerned with the efficient use of an important economic resource, namely, capital funds."* *-Solomon*

- *"Financial management is the operational activity of a business that is responsible for obtaining and effectively utilizing the funds necessary for efficient operation."* *-J. L. Massie*
- *"Financial management is an area of financial decision making harmonizing individual motives & enterprise goals."* *-Weston & Brigham*

- *"Financial management is the application of the planning and control functions of the finance function."*

  -Howard & Upton

- *"Financial management is the area of business management devoted to the judicious use of capital & careful selection of sources of capital in order to enable a spending unit to move in the direction of reaching its goals."*

  -J. F. Bradley

## 7.3 FEATURES OF FINANCIAL MANAGEMENT

On the basis of the above definitions, the following are the main characteristics of the financial management are shown in Fig. 7.1 and discussed below:

1. **Analytical thinking**: In this financial management financial problems are analyzed and considered. Study of trend of actual figures is made and ratio analysis is done.
2. **Continuous Process**: In past financial management was required rarely but now the financial manager remains busy throughout the year.
3. **Co-ordination between processes**: There is always a co-ordination between various processed of the business.
4. **Centralized nature**: Financial management is of a centralized nature. Other activities can be decentralized but there is only one department for financial management.

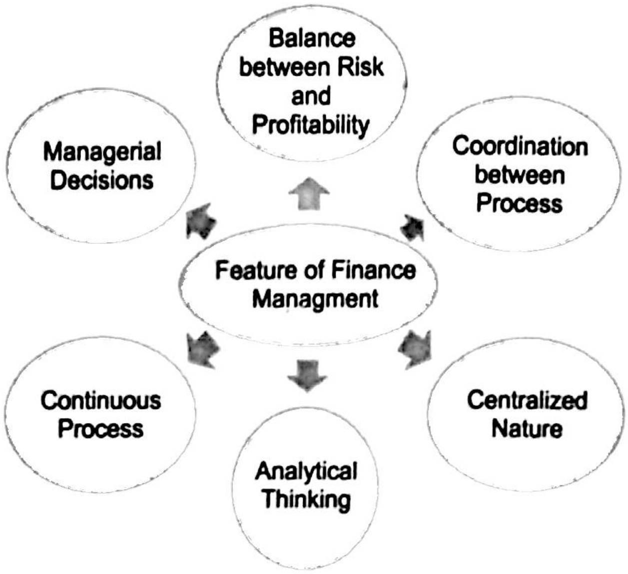


**Fig. 7.1** Features of Finance Management

5. **Managerial Decisions**: All managerial decisions relating to finance are taken after considering the report prepared by the finance manager. The financial management is the base of concrete managerial decisions.
6. **Maintaining Balance between Risk and Profitability**: The larger the risk in the business larger is the expectation of profits. Financial management maintain balance between the risk and profitability.

## 7.4 NATURE AND SCOPE

The nature and scope of financial management has undergone changes over the years. Until the middle of this century, its scope was limited to the funds under

major events in the life of the enterprise such as promotion, expansion, merger, etc.

As an integral part of the overall management, financial management is mainly concerned with achievement and use of funds by an organization. The following aspects are taken up in detail under the study of financial management:

- Determination of size of the enterprise and determination of rate of growth.
- Determining the composition of assets of the enterprise.
- Determining the mix of enterprise's financing, *i.e.*, consideration of level of debt to equity, etc.
- Analyze planning and control of financial affairs of the enterprise.

In the modern times, the financial management includes besides funds, the three different kinds of decisions as well namely:

(i) Investment.
(ii) Financing.
(iii) Dividend.

All the three types of decisions would be explained in detail during the course of this chapter. The given Fig. 7.2 gives the overview of the scope and functions of financial management. It also gives the inter-relation between the market value, financial decisions and risk return trade off.

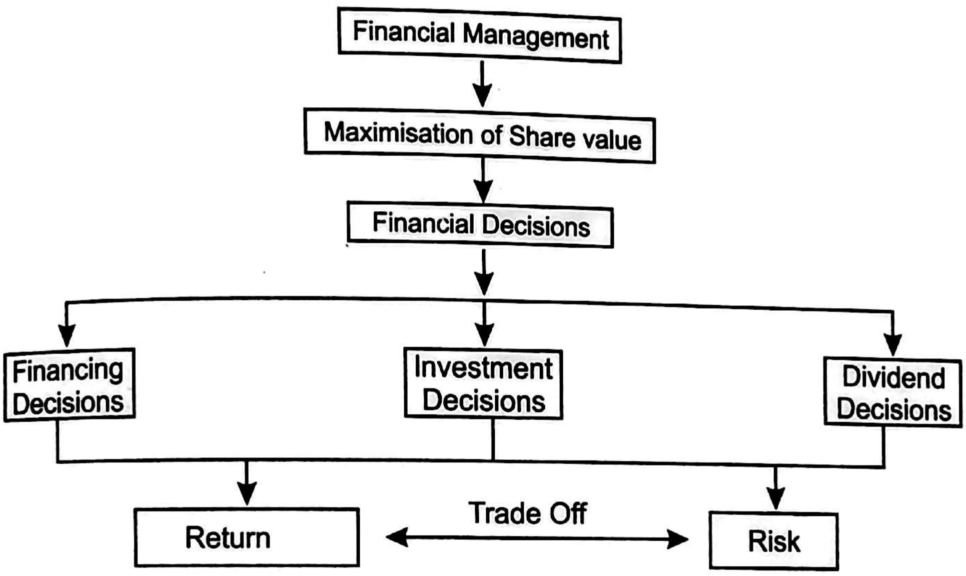


**Fig. 7.2** Nature and Scope of Finance Management

According to the above Figure 7.2, the financial manager, in a bid to maximize shareholders' wealth, should strive to maximize returns in relation to the given risk; he should seek courses of actions that avoid unnecessary risks. To ensure maximum return, funds flowing in and out of the firm should be constantly monitored to assure that they are safeguarded and properly utilized.

## 7.5 FORMS OF BUSINESS OWNERSHIP

Business concern are established with the objective of making profits. They can be established either by one person or by a group of persons in the private sector

by the government or other public bodies in the public sector. To start and select a sole proprietorship need business license for city, possibly a "fictitious name" statement, and a business checking account. The various forms of organization are established by state law. There are a wide variety of business organizations recognized by the states. For example, a popular form of organization is the Limited Liability Company (LLC). The LLC is a state designation. At the federal level, an LLC is taxed as a partnership. Some forms of business organizations are:

### 7.5.1 Sole Proprietor

The sole proprietorship is the oldest, simplest, and most common form of business entity. It is a business owned by a single individual. 'Sole' means single and 'proprietorship' means ownership. It means only one person or an individual becomes the owner of the business. Thus, the business organization in which a single person owns, manages and controls all the activities of the business is known as sole proprietorship form of business organization. The individual who owns and runs the sole proprietorship business is called a 'sole proprietor' or 'sole trader'. A sole proprietor pools and organizes the resources in a systematic way and controls the activities with the sole objective of earning profit.

***Features of Sole Proprietorship:***

The foregoing discussion reveals the following characteristics of sole proprietorship as shown in Fig. 7.3.

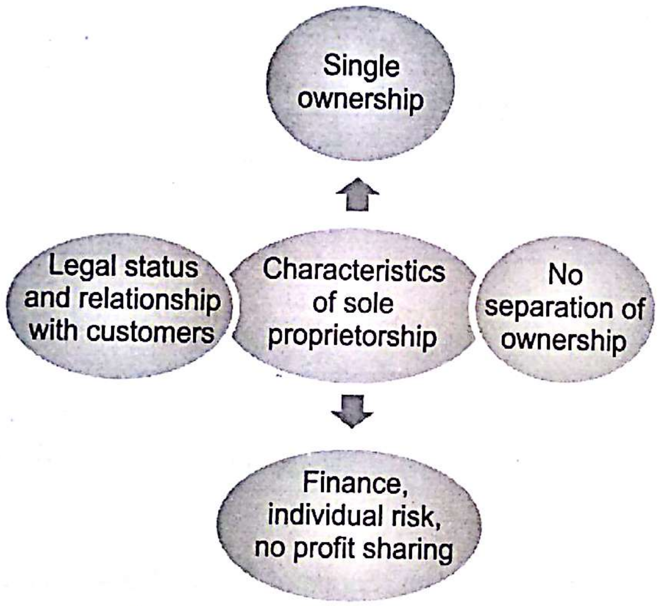


**Fig. 7.3** Characteristics of Sole Proprietorship

1. **Single Ownership**: A single individual always owns sole proprietorship form of business organization. That individual owns all assets and properties of the business. Consequently, he alone bears all the risk of the business. Thus, the business of the sole proprietor comes to an end at the will of the owner or upon his death.
2. **No separation of ownership from management**: There is no separation of ownership and management. The entrepreneur himself manages the business

and enjoy absolute control over the affairs of the business. He is the owner, manager, seller, purchaser and everything.

3. **Finance**: The necessary capital to run the business is provided by the sole owner. However, he may borrow from other sources such as friends or bank as need arises.
4. **Individual risk**: The entire risk of the business is born by the entrepreneur himself as he is the only owner of the business. All the risk and gain are the sole responsibility of the owner. This undivided risk will keep the entrepreneur vigilant and cautious for the business.
5. **No profit sharing**: The entrepreneur enjoys the entire profit earned in this form of business as there are no other persons to share the profit. Being the owner, he enjoys all the benefits.
6. **Legal status**: In law, the sole trader and his business are considered as one. In other words, all the assets and liabilities of the business are the personal assets and liabilities of the proprietor. It may be said that the owner and the business exist together.
7. **Relationship with customers**: The sole trader tries to keep good relationship with his customers. The customers are generally personally known to the proprietor and their orders are higher valued.

***Advantages of a Sole Proprietorship:***

Perhaps the greatest advantage of this form of business is its simplicity and low cost. It is neither required to file with the government, nor are any legal charter required. The sole proprietorship form of business has other advantages:

- The owner or proprietor is having complete control of business decisions.
- The income generated through operations can be directed into the proprietor's pocket or re-invested.
- Profits flow directly to the proprietor's personal tax return; they are not subject to a second level of taxation. In others words, profits from the business will not be taxed at the business level.
- The business can be dissolved as easily and informally as it was begun.
- These advantages account for the widespread adoption of the sole proprietorship in the India. Any person who wants to set up shop and begin dealing with customers can get right to it, in most cases without the intervention of government bureaucrats or lawyers.

***Disadvantages of the Sole Proprietorship:***

This legal form of organization, however, has following disadvantages:

- The amount of capital available to the business is limited to the owner's personal funds and whatever funds can be borrowed. This disadvantages limits the potential size of the business, no matter how attractive or popular its product or service.
- Sole proprietors have unlimited liability for all debts and legal judgments incurred in the course of business. Thus, a product liability lawsuit by a customer will not be made against the business but rather against the owner.

- The business may not be able to attract high-caliber employees whose goals include a share of business ownership. Sharing the benefits of ownership, other than simple profit-sharing, would require a change in the legal form of the business.
- Some employee benefits, such as owner's life, disability, and medical insurance premiums, may not be deductible, or may be only partially deductible from taxable income.

  The entity has a limited life; it exists only as long as the owner is alive. Upon the owner's death, the assets of the business go to his or her estate.

### 7.5.2 ▌Corporations

A corporation is a corporate body created by the special act of the parliament. Such act defines the power, duties, privileges and pattern of management of these organizations. Such an organisation is a statutory body to serve the general public. A public corporation is clothed with the power of the government, but possessed with flexibility and initiative of private enterprises. A public corporation enjoy complete autonomy in management.

***Features of corporation:***

The followings are some of the essential characteristics of public corporation:

1. It is a corporate body created by the special act in the state or central legislature. The power and duties of these corporations are defined by this act.
2. It enjoys the status of a legal entity and as such it can enter into contract in its own name.
3. It is completely owned by the government and as such no private individuals are entitled to purchase shares of these organizations.
4. A public corporation is managed by a board of directors. The members of the board are from all walks of industry and commerce. The chairperson of these corporations is appointed by the government.
5. The entire capital is financed by the government. It was set up with a capital of its own and is entitled to borrow, use and re-use revenue from the sale of goods.
6. A public corporation is primarily meant to render service and making profit is its secondary considerations.
7. The employees of corporation are subject to service conditions laid down by the corporation. Civil service rules for the government do not apply to the employees of the corporation.

### 7.5.3 ▌Partnership

Like corporations, partnerships are separate entities from the shareholders. To start a partnership, you will need an attorney to help you with the partnership agreement.

In simple words, a partnership is an association of two or more individuals who agree to carry on business together for the purpose of earning and sharing of profits. However a formal definition is provided by the Partnership Act of 1932.

***Features of Partnership:***

(i) **Simple procedure of formation:** The formation of partnership does not involve any complicated legal formalities. By an oral or written agreement, a partnership can be created. Even the registration of the agreement is not compulsory.

(ii) **Capital:** The capital of a partnership is contributed by the partners but it is not necessary that all the partners should contribute equally. Some may become partners without contributing any capital. This happens when such partners have special skills, abilities or experience. The partnership firm can also raise additional funds by borrowing from banks and others.

(iii) **Control:** The control is exercised jointly by all the partners. No major decision can be taken without consent of all the partners. However, in some firms, there may partners known as sleeping or dormant partners who do not take an active part in the conduct of the business.

(iv) **Management:** Every partner has a right to take part in the management of the firm. But generally, the partnership deed may provide that one or more than one partner will look after the management of the affairs of the firm. Sometimes the deed may provide for the division of responsibilities among the different partners depending upon their specialization.

(v) **Duration of partnership:** The duration of the partnership may be fixed or may not be fixed by the partners. In case duration is fixed, it is called as "partnership for a fixed term". When the fixed period is over, the partnership comes to an end.

### 7.5.4 ▌ Companies

A company is owned by shareholders who appoint Directors to give direction to the business. The Chief Executive is the senior official within the company with responsibility for making major decisions. Specialist managers will be appointed to run the company on behalf of the Board. A company is a legal body in its own right with an existence that is separate in law from its owners.

***Features of Companies:***

1. It is an artificial legal person created by law to achieve the objects for which it is formed. It has a nationality and domicile but cannot claim the fundamental rights expressly guaranteed to natural citizens and cannot do things that only a natural person can do. However, a company can challenge any law that violates the fundamental rights of citizens.
2. It has a distinct legal entity entirely independent of the members constituting it. No member can, either individually or jointly, claim any ownership rights in the assets of the company during its existence. In case of a section 25 company, this limitation is further extended and members do not receive any part of assets of the company even on its dissolution.
3. A company has perpetual succession and is not affected (in a legal sense) by changes in membership or employees, although such changes may affect its actual performance.
4. It also has the tremendous advantage of limited liability, which means that

members and executives are not personally liable to settle company's dues, unless they give their consent in writing for specific transactions.

5. Ownership and management are kept separate in a legal sense although in actual practice the two may be same.
6. Membership (ownership) rights are transferable. In case of a private company, certain restrictions are placed on this right to transfer membership.
7. A section 25 company cannot distribute profits or assets to its members.

### 7.5.5 Trusts

These are usually formed upon the death of an individual and are designed to provide continuity of the investments and business activities of the deceased individual. There are two statutes relevant to functioning of trusts in India: The Indian Trusts Act, 1882 and The Charitable and Religious Trusts Act, 1920.

***Characteristics of a trust:***

1. The obligation (created for forming the trust) must relate exclusively to property, the ownership of which vests with the trustees. An obligation, not so related, cannot be a trust. Moreover, unlike English law, the Indian law does not recognize duplicate ownership.
2. The obligation must arise out of confidence that is reposed in the trustee. Such confidence, in turn, must be accepted for the benefit of the beneficiaries.
3. A trust must be created for a lawful purpose.
4. The author of the trust must indicate with reasonable certainty the following:
   - Intention to create trust.
   - Purpose of the trust.
   - Beneficiaries of the trust, and
   - The trust property.

### 7.5.6 Elements Effects Selecting the Form of Organization

There are various environmental factors which can impact the selection of the form of organization. These environmental factors can be categorized into external and internal environment of the businesses. The internal environment of the company includes the factors which are within the company and under the control of company like: product organizational culture, leadership, and manufacturing (quality). On the other hand, the external factors are not under the control of the company and include: social environment, political conditions, suppliers, competitors of the company, government regulations and policies, accounting agencies like accounting standard board. Some major factor is as following:

1. **Political factors:** These refer to government policy such as the degree of intervention in the economy. What goods and services does a government want to provide? To what extent does it believe in subsidizing firms? What are its priorities in terms of business support? Political decisions can impact on many vital areas for business such as the education of the workforce, the health of the nation and the quality of the infrastructure of the economy such as the road and rail system.

2. **Economic factors:** These include interest rates, taxation changes, economic growth, inflation and exchange rates. For example:
   - Higher interest rates may discourage investment because it costs more to borrow
   - A strong currency may make exporting more difficult because it may raise the price in terms of foreign currency. Inflation may provoke higher wage demands from employees and raise costs.
   - Higher national income growth may boost demand for a firm's products.
3. **Social factors:** Changes in social trends can impact on the demand for a firm's products and the availability and willingness of individuals to work. In India, for example, the population has been ageing. The ageing population also has impact on demand. For example, demand for sheltered accommodation and medicines have increased whereas demand for toys is falling.
4. **Technological factors:** New technologies create new products and new processes. MP3 players, computer games, online gambling and high definition TVs are all new markets created by technological advances. Online shopping, bar coding and computer aided design are all improvements in the way of doing business as a result of better technology. Technology can reduce costs, improve quality and lead to innovation. These developments can benefit consumers as well as the organizations providing the products.

## 7.6 BALANCE SHEET

A balance sheet must balance the assets, liabilities and owner's equity. Most commonly, the assets are on top and the liabilities and owner's equity on the bottom. A balance sheet, also called the statement of financial position that consist of:

- Assets
- Liabilities
- Owners Equity

As of a specific date it gives an idea of what the company is worth.

**Important Point:** *A financial statement that summarizes a company's assets, liabilities and shareholders' equity at a specific point in time.*

The balance sheet of a business possesses the following characteristics:

Balance sheet being a statement has no 'debit' or 'credit' sides that is why 'To' or 'By' words are not prefixed to the name of accounts. Balance sheet is prepared at the end of an accounting period-it is for a particular day, so it discloses the financial position on a particular day and not for a particular period for example: Balance Sheet of XYZ Ltd., as on March 31, 2013.

Balance sheet discloses how much business owes to others and how much others owe to business. The total of Assets and Liabilities sides are always equal.

### 7.6.1 Elements of balance sheet

1. **Assets (in):** Assets are all those things a company owns which are of value to the business. Assets can be tangible like *e.g.*, a manufacturing plant, computers, fixed deposits or cash in the bank. Tangible assets like cash or goods for sale that can easily (*i.e.*, within an accounting year) be converted into cash are called current assets while other assets like properties and equipment are called fixed assets. Assets can also be intangible like *e.g.*, copyrights and patent.
2. **Liabilities (out):** Liabilities are all those things for which the company eventually needs to pay. There are two types of liabilities:

   Current Liabilities need to be paid within one accounting year. Examples are: Outstanding rent, goods bought on credit.

   Long term liabilities are those liabilities which will not be paid during the current accounting year. Examples are: Long term debts, bank loans.
3. **Owner's Equity (?):** Owner's equity is by definition the difference between the assets of a company and its liabilities.

$$\text{Owner's Equity} = \text{Assets} - \text{Liabilities}$$

Owner's Equity is divided into two parts:

(1) **Contributed Capital.** This is the money that the owners invested in the company.

(2) **Retained Earnings.** Those earnings which were not distributed to the owners as dividends. These can accumulate to a large sum over the years.

A simple example of balance sheet shown in Fig. 7.4.

**Balance Sheet as on March 31, 2012**

| **Assets** | |
|---|---|
| Cash and Equivalents | 10000 |
| Accounts Receivable | 1200 |
| Inventory | 8300 |
| Total Current Assets | 19500 |
| Plant and Equipment | 800 |
| Accumulated Depreciation | 500 |
| Net Fixed assets | 300 |
| **Total Assets** | **19800** |
| **Liabilities and Owner's Equity** | |
| Accounts Payble | 7600 |
| Other Current Liabilities | 900 |
| Total Current Liabilities | 8500 |
| Long Term Debt | 1200 |
| Total Liabilities | 9700 |
| Common Stock | 6000 |
| Retained Earnings | 4100 |
| Total Shareholder's Equity | 10100 |
| **Total Liabilities and owner's Equity** | **19800** |

Same

*It's a Balance Sheet*

**Fig. 7.4** A simple Balance Sheet

## 7.7 PROFIT AND LOSS ACCOUNT

A profit and loss account is produced primarily for business purposes – to show owners, shareholders or potential investors how the business is performing. But most of the information is also used by the Inland Revenue to work out your tax bill. The profit and loss statement shows the trading performance of the business and the distribution of profit.

**Important Point:** *A profit and loss account is a summary of business transactions for a given period - normally 12 months. By deducting total expenditure from total income, it shows on the "bottom line".*

The purpose of the profit and loss account is to:

It show whether a business has made a PROFIT or LOSS over a financial year.

Describe how the profit or loss arose – *e.g.*, categorizing costs between "cost of sales" and "operating costs".

A profit and loss account starts with the **Trading Account** and then takes into account all the other expenses associated with the business.

(i) **Trading Account:** That part of the profit and loss account where the cost of goods sold is compared with the money raised by their sale to arrive at the gross profit. This gives a view of the business in terms of sales and viability of profit. Trading account for XYZ place for the year ended March 31, 2012 is shown in Table 7.1.

**Table 7.1 Trading Account for XYZ place**

| Category | Rs. | Rs. |
|---|---|---|
| Sales | | 12,00,000 |
| Opening Stock | 150,000 | |
| Purchases | 400,000 | |
| less Closing Stock | 220,000 | |
| Cost of Sales | 330,000 | (330,000) |
| Other Costs | | (70,000) |
| Gross Profit | | 800,000 |

Note that the closing stock figure would appear in the balance sheet under Stock. The trading account now has all the other expenses now deducted. It would look like the Table 7.2 below:

**Table 7.2 Profit and loss account for XYZ place for the year ended March 31, 2012**

| | | Rs. | Examples |
|---|---|---|---|
| Turnover (sales) revenue | 12,00,000 | The amount of money generated by sales. | e.g. 400 cars at 3,000 each |
| Cost of Sales | 400 | The cost of making the goods or buying them. | Raw materials. Cost of labour working directly on each product. |

| | | | |
|---|---|---|---|
| | | | Cost of running the machines/equipment. |
| **Gross profit** | 800 | Turnover minus cost of sales. | Cost of premises *e.g.*, rent, |
| **Overheads or expenses** | 320 | Costs not directly involved in the production process (indirect costs) | insurance, repairs Office costs *e.g.*, stationery, postage, computer maintenance, staff salaries and wages sales and marketing costs *e.g.*, salaries of salesmen, advertising Finance costs e.g. bank charges, interest on bank loans |
| **Operating profit** | 480 | Gross Profit minus overheads Also know as NET PROFIT | |
| **Interest and taxation payable** | 200 | The money that is due to be paid in interest on loans and to the Inland Revenue as tax | |
| **Net profit after tax and interest** | 280 | The money available to be distributed to shareholders | |
| **Dividends** | 170 | Money paid to shareholders as a reward for holding shares | |
| **Retained profit** | 90 | The money left for the business to reinvest | |

The business has to pay tax at the rate determined by the government and interest at the rates determined by the lenders.

(ii) **Manufacturing Account:** Many business entities engage in manufacturing activities and this involves the purchasing of raw materials and incurring labour and other cost in converting the raw materials into finished goods. For this purpose a manufacturing account is prepared in order to ascertain the cost of producing the goods. This account is also normally prepared at the end of the accounting period. Both direct and indirect expenses associated with the manufacturing process debited to the manufacturing account. The balance of this account representing cost of the goods produced is then transferred to the trading account. The order of presentation of the final accounts is as under:

(a) Manufacturing account
(b) Trading account
(c) Profit and loss account
(d) Profit and loss appropriation account
(e) Balance sheet.

| | | | | | |
|---|---|---|---|---|---|
| **Direct Materials** | | | Closing Stock: | | |
| Opening Stock: | | | Raw Materials | X | |
| Raw Materials | X | G | Work-in-Progress | X | X |
| Work-in-Progress | X | X | Cost of the goods | | |

| | | | | |
|---|---|---|---|---|
| Purchases: | | | transferred to Trading | |
| Work-in-Progress | | | | |
| Raw Materials | X | | Account | |
| Carriage inwards | | X | | X |
| Direact Labour | | | | |
| Factory wages | | X | | |
| Direct Expense | | | | |
| Factory rent | X | | | |
| Fuel, power, gas, etc. | X | | | |
| Factory Insurance | X | | | |
| Depreciation on | | | | |
| Factory Building | | | | |
| etc. | X | XX | | |
| Manufacturing over-heads | | XX | | |
| | | XX | | XX |

(iii) **Yearly Profit and Loss:** By law, if your business is a limited company or a partnership whose members are limited companies, you must produce a profit and loss account for each financial year. Self employed sole traders and most partnerships do not need to create a formal profit and loss account-the information they complete on the self assessment tax return form amounts to the same thing.

However, there are key benefits to producing formal accounts. If you are looking to grow your business, or need a loan or mortgage, for example, most institutions will ask to see last consecutive three years accounts.

(iv) **Keeping accurate records:** By law business must keep accurate records of income and expenditure. Keep self-employment records for five years and limited company/partnership records for six years after the latest date your tax return is due accurate record keeping has following important benefits:

- It gives information to manage your business and make it grow.
- Enables reporting on profit/loss easily and quickly when required.
- It will improve your chances of getting a loan or mortgage.
- It makes filling in your tax return easier and quicker.
- It helps you or your company avoid paying too much tax.
- This provides back-up for claims for certain allowances.
- This helps you plan and budget for tax payments.
- It prevents interest or penalties for late tax payments.
- It helps reduce accountant fees - your annual accounts will be far easier to produce.

## 7.8 WORKING CAPITAL

The capital which is required to finance current assets is called working capital. That is in operating daily or day-to-day business of the firm effectively, some

resources are needed and the capital which are needed to finance, these resources are called working capital.

**Important Point:** *"Working capital may be defined as all the short term assets used in daily operation".*

*—John. J Harpton.*

Short term assets of a firm means cash money, short-term securities, inventory, bill receivable, note receivable, debtors, etc. In operating daily business, fixed assets are also needed in addition to current assets.

Working capital is a measure of both a company's efficiency and its short-term financial health. The working capital is calculated as the difference between current assets and current liabilities.

**Working Capital = Current Assets – Current Liabilities**

***Current assets include:***

- Stock of raw material.
- Stock of work-in-progress.
- Stock of finished goods.
- Sundry debtors and bills receivables.
- Prepaid expenses.
- Accrued incomes.
- Cash in bank.

***Current liabilities include:***

- Creditors for materials.
- Creditors for wages and other expenses.
- Bills payable.
- Bank overdraft.

### 7.8.1 Under Capitalization

In general under-capitalization denotes the inadequacy of capital; *i.e.*, the shortage of capital. It is a condition when the real value of the company based on its earnings is more than the book value.

Under-capitalization refers to any situation where a business cannot acquire the funds they need. An under-capitalized business may be one that cannot afford current operational expenses due to a lack of capital, which can trigger bankruptcy, may be one that is over-exposed to risk, or may be one that is financially sound but does not have the funds required to expand to meet market demand.

**Important Point:** *"A corporation may be under-capitalized when the rate of profits is making on the total capital is exceptionally high in relation to the return enjoyed by similarly situated companies in the same industry, or when it has too little capital with which to conduct its business."*

*-Charles W. Gerstenberg*

Under-capitalization is often a result of improper financial planning. However, a viable business may have difficulty raising sufficient capital during an economic downturn or in a country that imposes artificial constraints on capital investment. There are several different causes of undercapitalization including:

- Financing growth with short-term capital, rather than permanent capital
- Failing to secure an adequate bank loan at a critical time
- Failing to obtain insurance against predictable business risks
- Adverse macro-economic conditions.

### 7.8.2 Over Capitalization

In general over-capitalization implies that the capital of the company exceeds its requirements. A corporation (company) is overcapitalized when its earnings are not enough to yield a fair return on the amounts of stocks and bonds that have been issued or when the amount of securities outstanding exceeds the current value of the assets.

**Important Point:** *"Whenever the aggregate of the par value of stocks and bonds outstanding exceed the true value of its assets, the corporation company is said to be over-capitalized."*

*- Hoagland*

The main causes of over-capitalization are:

- Promotion of company with overvalued assets.
- Purchase of assets during boom period, *i.e.*, at higher prices.
- High promotional expenses.
- Raising excessive capital, *i.e.*, more capital than what it can profitably use.
- Borrowing money at high rates of interest.
- Over-estimation of earnings.
- High rate taxation.
- Liberal dividend policy, etc.

## 7.9 FUND FLOW AND CASH FLOW STATEMENTS

Fund flow statements explains changes in funds or changes in working capital and also explains the working capital position of the company which gives an idea to the top management about the liquidity position of the company.

Steps in preparation of funds flow statement:

(i) Preparation of working capital statement that explains increase or decrease in working capital.

(ii) Preparation of funds from operation statement in which we find out operating profit.

(iii) Preparation of funds flow statement that shows various sources and application of fund as shown in Fig. 7.5.

Cash flow statement (CFS) depicting change in cash possession from one period to another. It explains the reasons for inflows or outflows of cash.

The steps in preparation of cash flow statement are: Statement of cash from operation in this we may find out the cash profit of the company. Preparation of cash flow statement in which we will explain various in flows and out flows of cash. Here we will take the opening cash balance of the company and add various inflows to it and deduct various outflows. Finally we will get the closing cash balance of the company.

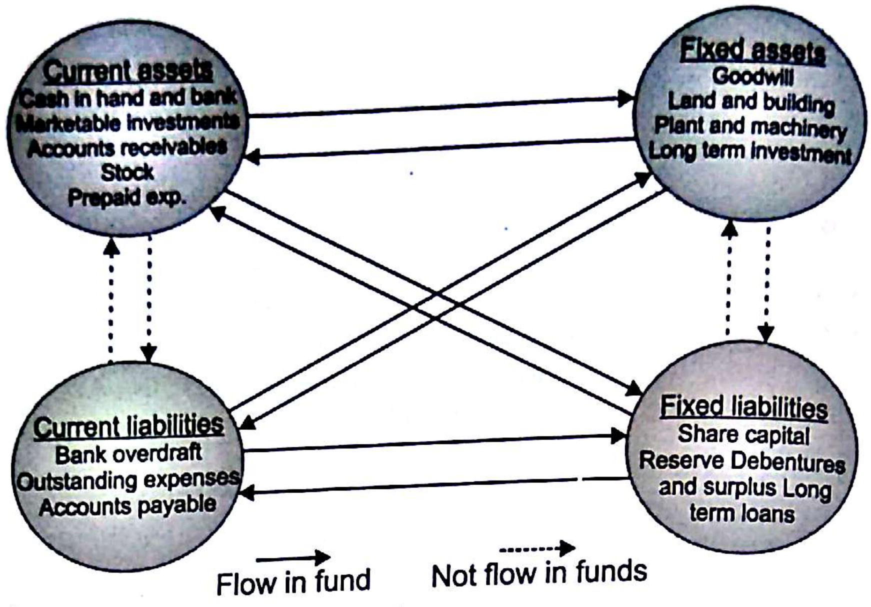


**Fig. 7.5** Flow of funds

Uses of Cash Flow Statement:

- Helps in efficient cash management
- Helps in internal financial management
- Discloses the movement of cash
- Discloses success or failure of cash planning.

**Analyzing an Example of a CFS:** Let's take a look at this CFS sample in following Table 7.3:

**Table 7.3**

| **Cash Flow Statement<br>Company XYZ<br>Fy Ended 31 Dec 2012** | |
|---|---|
| **Cash Flow Form Operations** | |
| Net Earnings | 2,000,000 |
| *Additions to Cash* | |
| Depreciation | 10,000 |
| Decrease in Accounts Receivable | 15,000 |
| Increase in Accounts Payable | 15,000 |
| Increase in Taxes Payable | 2,000 |
| *Subtractions From Cash* | |
| Increase in Inventory | (30,000) |
| Net Cash From Operations | 2,012,000 |
| **Cash Flow From Investing** | (500,000) |
| Equipment | |
| **Cash Flow Form Financing** | |
| **Notes Payable** | **10,000** |
| **Cash Flow for F.Y Ended 31 Dec 2012** | **15,22,000** |

From this CFS, we can see that the cash flow for FY 2012 was 15,22,000. The bulk of the positive cash flow statement from cash earned from operations, which is a good sign for investors. It means that core operations are generating business and that there is enough money to buy new inventory. The purchasing of new equipment shows that the company has cash to invest in inventory for growth. Finally, the amount of cash available to the company should ease investors' minds regarding the notes payable, as cash is plentiful to cover that future loan expense.

### 7.9.1 Difference between Fund Flow and Cash Flow Statement

Many people think that both cash and fund are same, however they both are different and so it is the case with cash flow statement and funds flow statement. A difference between these two statements may be briefed as under:

| S.No. | Fund Flow Statement | Cash Flow Statement |
|---|---|---|
| 1. | Fund flow statement is based on broader concept *i.e.*, working capital. | Cash flow statement is based on narrow concept *i.e.*, Cash which is only one of the elements of working capital. |
| 2. | Funds Flow Statement is concerned with all items constituting funds (Working Capital) for the business. | Cash Flow Statement deals only with cash transactions. |
| 3. | A transaction affecting working capital other than cash will affect Funds Flow Statement. | A transaction affecting working capital other than cash will not affect the Cash Flow Statement |
| 4. | In funds flow statement, net increase or decrease in working capital is recorded. | In cash flow statement, individual item involving cash is taken into account. |
| 5. | In funds flow statement there is no classification. | In cash flow statement there is classification of cash flows as: <br>• Cash flow from operating activities, <br>• Cash flow from investment activities and <br>• Cash flow from financing activities. |

### 7.9.2 Difference between Balance Sheet and Funds Flow Statement

There is also a difference between meaning and purpose of funds flow statement and balance sheet although both are prepared with the same accounting data. A difference between these two may be briefed as under:

| S.No. | Balance Sheet | Funds Flow Statement |
|---|---|---|
| 1. | Balance sheet is a statement showing the financial position of the concern on a particular date. The asset side portrays the development of resources in various types of properties and liabilities side indicates the manner in which these resources are obtained. It shows all assets and liabilities whether current or fixed, tangible or intangible, etc. | Funds flow statement shows the changes in current assets and current liabilities during a particular period of time. |
| 2. | Balance sheet shows the total financial position on a particular date and in this way, it is of a historical nature and therefore, its utility is very limited for the management. | On the other hand, funds flow statement is a comparative statement of assets and liabilities and depicts the changes in working capital during the period of two balance sheets. |
| 3. | Balance sheet represents the balance of various assets and liabilities and does not present analysis of any kind. | Funds flow statement is an analysis and control device for the management. Management can ensure the long term and short term solvency of the firm by studying the internal funds flow cycles. It is a modern technique of knowing the inflows and outflows of funds during a particular period. |

## 7.10 BREAK EVEN POINT (B.E.P)

The break-even point is the volume of sales you need to cover your costs and no profit and no loss is made. It is a zero profit point. The break-even point can be a very useful management tool because it enables a manager to determine:

- The profitability of the present product line.
- How far sales can decline before losses are incurred?
- How many units have to be sold before it becomes profitable?
- What effects a reduction in selling price or the volume of sales will have on the profitability of the business?
- What the effect on profitability will be if overhead expenses increase?
- How much more has to be sold at current price levels to make up for an increase in the cost of sales?
- Calculation of the break-even point.

**Important Point:** *The break-even point (BEP) is the point at which cost or expenses and revenue are equal: there is no net loss or gain, and one has "broken even". A profit or a loss has not been made, although opportunity costs have been "paid", and capital has received the risk-adjusted, expected return.*

Thus, Break Even Point is the point where Total Cost = Total Revenue

Assumptions in Break Even Point

The assumptions underlying break-even point are:

- Prices remain fixed.
- Variable cost rate will remain fixed.
- Total fixed costs will remain fixed up to maximum manufacturing capacity of the firm.
- Quantity of units produced is equal to quantity of units sold, so there is no change in inventory.
- Costs can be classified accurately as either fixed or variable.
- Changes in activity are the only factors that affect costs.
- When a company sells more than one type of product, the sales mix (the ratio of each product to total sales) will remain constant.

There are two ways of calculating the break even point, in units and in sales revenue.

1. The break-even point (in terms of Unit Sales (X)) can be directly computed as follows:

$$\text{Break Even Point (in Units)} = \frac{\text{Total Fixed Cost}}{(\text{Selling Price} - \text{Variable Cost})}$$

Or

$$\text{BEP (in Units)} = \frac{\text{Total Fixed Cost}}{\text{Contribution Margin}}$$

Where, Contribution Margin = (Selling Price per unit – Variable Cost per unit)

2. In currency units (sales proceeds) to reach break-even, one can use the above calculation and multiply by Price (P), or equivalently use the Contribution Margin Ratio (Unit Contribution Margin over Price) to compute it in terms of value.

$$\text{BEP (in value)} = \frac{\text{Total Fixed Cost}}{\text{Contribution Margin}} \times \text{Price per unit}$$

For example ABC Ltd expects to sell 10000 units at 10 each. The variable cost per unit is Rs.5/- and the fixed cost is Rs.15,000/- per annum. Calculate the break even point in units and in sale revenue.

To calculate the BEP in units you would use the formula fixed cost divided by contribution per unit. Therefore you would divide 15000 by contribution which is selling price 10 minus variable cost per unit 5. 15000 divided by 5. The final answer is 3000 units.

In terms of sales revenue you would divide the fixed cost by the c/s ratio. 15000 divided by (contribution divided by selling price per unit). 15000 divided by (5 divided by 10).15000 divided by 0.5. The final answer is 30000. And we know this is the correct answer because when we multiply the break even point in units by the selling price we get the same answer. Let's look at the example using a graph as shown in the Fig. 7.6.

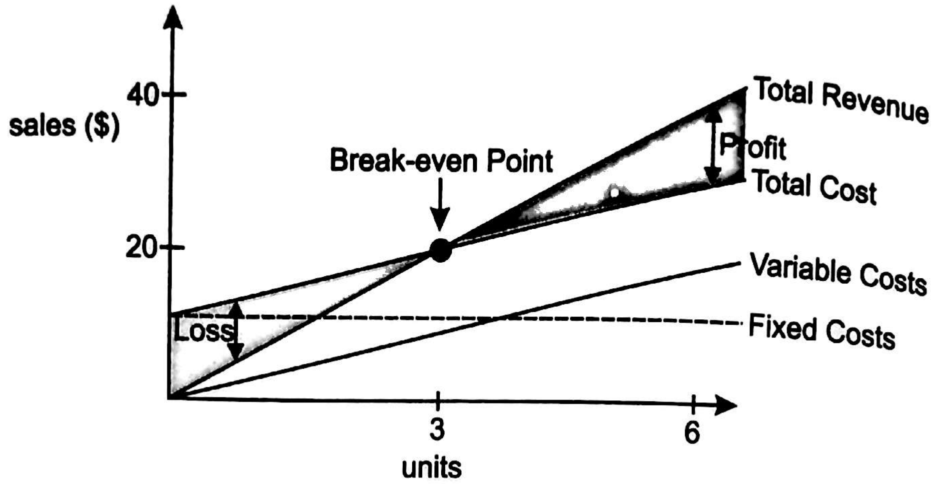


**Fig.7.6 BEP**

A break even chart is a graphical representation of the break even point, profits, losses and also margin of safety.

***Limitations of Break Even Point***

Break-even analysis is only a supply side (*i.e.*, costs only) analysis, as it tells you nothing about what sales are actually likely to be for the product at these various prices.

It assumes that fixed costs are constant. Although this is true in the short run, an increase in the scale of production is likely to cause fixed costs to rise.

It assumes average variable costs are constant per unit of output, at least in the range of likely quantities of sales. (*i.e.*, linearity)

It assumes that the quantity of goods produced is equal to the quantity of goods sold (*i.e.*, there is no change in the quantity of goods held in inventory at the beginning of the period and the quantity of goods held in inventory at the end of the period).

In multi-product companies, it assumes that the relative proportions of each product sold and produced are constant (*i.e.*, the sales mix is constant).

## 7.11 FINANCIAL RATIO ANALYSIS

Ratio analysis is the method or process by which the relationship of items or groups of items in the financial statements are computed, determined and presented. Ratio analysis is an attempt to derive quantitative measures or guides concerning the financial health and profitability of the business enterprise. Ratio analysis can be used both in trend and static analysis.

**Important Point:** *Ratio analysis is defined as the systematic use of ratios to interpret the financial statements so that the strengths and weaknesses of a firm as well as its historical performance and current financial condition can be determined the term ratio refers to the numerical or quantitative relationship between items/variables.*

This relationship can be expressed as:

(1) Fraction

(2) Percentages

(3) Proportion of numbers

For example, the fraction $\frac{2}{5}$ can be represented as a different fracton $\left(\frac{4}{10}\right)$, as a decimal (0.4) or as a percentage (40%). Consumers often see signs advertising $\frac{1}{2}$ price or 50% off. These two forms mean the same thing they are simply different ways of expressing parts of a whole.

These alternative methods of expressing items which are related to each other are, for purposes of financial analysis, referred to as ratio analysis. It should be noted that computing the ratio does not add any information in the figures of profit or sales. What the ratios do is that they reveal the relationship in a more meaningful way so as to enable us to draw conclusions from them. Financial ratios are often divided into categories based on the information that they provide:

1. **Liquidity ratios.** Liquidity refers to the speed with which an asset can be converted to cash. Liquidity ratios describe the ability of a firm to meet its current obligations. There are three common liquidity ratios: Current Ratio, Quick Ratio and Cash Ratio. The formula of cash ratio is as following:

Formula:

$$\text{Cash Ratio} = \frac{\text{Cash}}{\text{Current Liabilities}}$$

2. **Efficiency ratios.** The efficiency ratios describe how well a firm is using its investment in various asset classes with their formula:

   **(i) Inventory Turnover Ratio or Stock Turnover Ratio:** The inventory turnover formula or stock turnover ratio is the number of times that inventory is used during a measurement period (usually a year). The most simple inventory turnover calculation is to divide the period-end inventory into the annualized cost of sales. You can also use an average inventory figure in the denominator, which avoids sudden changes in the inventory level that are likely to occur on any specific period-end date. The formula is as follows:

$$\text{Inventory Turnover} = \frac{\text{Cost of Goods Sold}}{\text{Inventory}}$$

   **(ii) Accounts Receivable Turnover Ratio (A/R):** The receivable turnover ratio (debtors turnover ratio, accounts receivable turnover ratio) indicates the velocity of a company's debt collection, the number of times average receivables are turned over during a year.

$$\text{A/R Turnover} = \frac{\text{Annual Credit Sales}}{\text{Accounts Recievable}}$$

   **(iii) Average Collection Period (ACP):** Average Collection Period represents the average number of days it takes the company to convert receivables into cash. Average Collection Period formula is:

$$\text{Average Collection Period} = \frac{365}{\text{Receivable Turnover Ration}}$$

(iv) **Fixed Asset Turnover Ratio (FATR):** Fixed asset turnover ratio compares the sales revenue a company to its fixed assets. This ratio tell us how effectively and efficiently a company is using its fixed assets to generate revenues. The formula is as follows:

$$\text{Total Asset Turnover} = \frac{\text{Sales}}{\text{Net Fixed Assets}}$$

(v) **Total Asset Turnover Ratio (TATR):** This ratio considers all assets, current and fixed. Those assets include fixed assets, like plant and equipment, as well as inventory, accounts receivable, as well as any other current assets. The formula is as follows:

$$\text{Total Asset Turnover} = \frac{\text{Sales}}{\text{Total cost}}$$

3. **Leverage ratios.** Leverage ratios describe the amount of debt that the firm has used to finance its investments in assets and can be explained with the following formula:

(i) **Total Debt Ratio (TDR):** The Total debt ratio takes into account all debts to all creditors. The formula is as follows:

$$\text{Total Debt Ratio} = \frac{\text{Total Liabilities}}{\text{Total Assets}}$$

(ii) **Long-term Debt Ratio (LTDR):** Calculated as long-term debt divided by total assets. A firm's debt capacity for its working capital structure is determined this way. The formula is as follows.

$$\text{Long term Debt Ratio} = \frac{\text{Long term Debt}}{\text{Total Assets}}$$

(iii) **Debt to Equity (DE):** The debt-to-equity ratio is a measure of the relationship between the capital contributed by creditors and the capital contributed by shareholders. It also shows the extent to which shareholders' equity can fulfill a company's obligations to creditors in the event of liquidation. The formula is as follows:

$$\text{Debt to Equity} = \frac{\text{Total Liabilities}}{\text{Total Equity}}$$

(iv) **Long-term Debt to Equity (LTD).** It expresses the relationship between long-term capital contributions of creditors as related to that contributed by owners (investors). The formula is as follows:

$$\text{LTD to Equity} = \frac{\text{Long term Debt}}{\text{Total Equity}}$$

4. **Coverage.** Coverage ratios indicate the firm's ability to pay certain expenses:

(i) **Times Interest Earned Ratio (TIE):** Times interest earned or interest coverage ratio is the ratio of earnings before interest and tax (EBIT) of a business to its interest expense during a period. It is a solvency ratio

measuring the long term viability of a business to pay off its debts. The formula is as follows:

$$\text{TIE} = \frac{\text{EBIT}}{\text{Interst Expense}}$$

(ii) **Cash Coverage Ratio (CCR):** The cash coverage ratio is useful for determining the amount of cash available to pay for interest, and is expressed as a ratio of the cash available to the amount of interest to be paid. The formula is as follows:

$$\text{Cash Coverage Ratio} = \frac{\text{EBIT + Non cash Expenses}}{\text{Interest Expense}}$$

## 7.12 CAPITAL BUDGETING

Capital budgeting is the process by which the firm decides which long-term investments to make. Capital budgeting projects, *i.e.*, potential long-term investments, are expected to generate cash flows over several years. The decision to accept or reject a capital budgeting project depends on an analysis of the cash flows generated by the project and its cost. The following three capital budgeting decision rules will be presented:

- Payback Period
- Net Present Value (NPV)
- Internal Rate of Return (IRR)

A capital budgeting decision rule should satisfy the following criteria:

- Must consider all of the project's cash flows.
- Must consider the Time Value Capital Budgeting of Money
- Must always lead to the correct decision when choosing among Mutually Exclusive Projects.

### 7.12.1 Payback Period (PP)

Payback period is the time in which the initial cash outflow of an investment is expected to be recovered from the cash inflows generated by the investment. It is one of the simplest investment appraisal techniques. The formula to calculate payback period of a project depends on whether the cash flow per period from the project is even or uneven. In case the cash flow per period are even, the formula to calculate payback period is:

$$\text{Payback Period} = \frac{\text{Initial Investment}}{\text{Cash Inflow per Period}}$$

When cash inflows are uneven, we need to calculate the cumulative net cash flow for each period and then use the following formula for payback period:

$$\text{Payback Period} = A + \frac{B}{C}$$

In the above formula,

A = Last period with a negative cumulative cash flow;

B = Absolute value of cumulative cash flow at the end of the period A;

C = Actual Cash Flow during the period after A

**Example-1. Even Cash Flows.** Company C is planning to undertake a project requiring initial investment of 100 million. The project is expected to generate 25 million per year for 10 years. Calculate the payback period of the project.

**Solution**–Payback Period = Initial Investment/Annual Cash Flow = 100M/25M = 4 years

**Advantages:**

1. Payback period is quite simple to calculate.
2. It can be a measure of risk inherent in a project. Since, cash flows that occur later in a project's life are considered more uncertain, payback period provides an indication of certain project cash inflows are.
3. For companies facing liquidity problems, it provides a good ranking of projects that would return money early.

**Disadvantage:**

1. Payback period does not take into account the time value of money which is a serious drawback since it could lead to wrong decisions. A variation of payback method that attempts to remove this drawback is called discounted payback period method.
2. It does not take into account, the cash flows that occur after the payback period is reached.

### 7.12.2 ▌ Net Present Value (NPV)

A present value is the value now of a stream of future cash flows, negative or positive. The value of each cash flow needs to be adjusted for risk and the time value of money.

In general, present value (PV) refers to the value now of payments to be received in the future (I). The present value of I after n year at r is:

> **Important Point:** *A net present value (NPV) includes all cash flows including initial cash flows such as the cost of purchasing an asset, whereas a present value does not. The simple present value is useful where the negative cash flow is an initial one-off, as when buying a security.*
>
> ▪ *The net present value (NPV) or net present worth (NPW) of a time series of cash flows, both incoming and outgoing, is defined as the sum of the present values (PVs) of the individual cash flows of the same entity.*

Net present value is one of the most reliable measure used in capital budgeting. It is the present value of net cash inflows generated by a project less the initial investment on the project. The use of discounted cash inflows means that net present value accounts for time value of money. Before calculating NPV, a target rate of return is set which is used to discount the net cash inflows from a project.

The major component of NPV is the present value of net cash inflows which may be even (*i.e.*, equal cash inflows in different periods) or uneven (*i.e.*, different cash flows in different periods). Where net cash inflows are even, present value

can be easily calculated by using the present value formula of annuity. However if net cash inflows are uneven we need to calculate the present value of each individual cash inflow separately. Thus we have two formulas for the calculating of NPV:

**When cash inflows are Even:**

$$\text{NPV} = R \times \frac{1-(1+i)^{-n}}{i} - \text{Intial Investment}$$

In the above formula,

- R is the net cash inflow expected to be received each period.
- i is the required rate of return per period.
- n are the number of periods during which the project is expected to operate and generate cash inflows.

**When cash inflows are uneven:**

$$\text{NPV} = \left[\frac{R_1}{(1+i)^1} + \frac{R_2}{(1+i)^2} + \frac{R_3}{(1+i)^3} + \ldots\right] - \text{Initial Investment}$$

Where,

- i is the target rate of return per period.
- $R_1$ is the net cash inflow during the first period.
- $R_2$ is the net cash inflow during the second period.
- $R_3$ is the net cash inflow during the third period, and so on.

***Advantage and Disadvantage of NPV***

**Advantage:** Net present value accounts for time value of money. Thus it is more reliable than other investment appraisal techniques such payback period and accounting rate of return. Also it is fairly easy to calculate.

**Disadvantage:** It is based on estimated future cash flows of the project and estimates may be far from actual results.

### 7.12.3 ▮ Internal Rate of Return (IRR)

The internal rate of return (IRR) or economic rate of return (ERR) is a rate of return used in capital budgeting to measure and compare the profitability of investments.

**Important Point:** *Internal rate of return (IRR) is the interest rate at which the net present value of all the cash flows (both positive and negative) from a project or investment equal zero.*

The calculation of IRR is a bit complex than other capital budgeting techniques. We know that at IRR, Net Present Value (NPV) is zero, thus:

NPV = 0; or

PV of future cash flows—Initial Investment = 0; or

$$\left[\frac{CF_1}{(1+r)^1} + \frac{CF_2}{(1+r)^2} + \frac{CF_3}{(1+r)^3} + \ldots\right] - \text{Initial Investment} = 0$$

Where,

- r is the internal rate of return;
- $CF_1$ is the period one net cash inflow;
- $CF_2$ is the period two net cash inflow,
- $CF_3$ is the period three net cash inflow, and so on ...

But the problem is, we cannot isolate the variable r (=internal rate of return) on one side of the above equation. However, there are alternative procedures which can be followed to find IRR. The simplest of them is described below:

1. Guess the value of r and calculate the NPV of the project at that value.
2. If NPV is close to zero then IRR is equal to r.
3. If NPV is greater than 0 then increase r and jump to step 5.
4. If NPV is smaller than 0 then decrease r and jump to step 5.
5. Recalculate NPV using the new value of r and go back to step 2.

**Example:** Find the IRR of an investment having initial cash outflow of Rs. 2,13,000/-. The cash inflows during the first, second, third and fourth years are expected to be Rs. 65,200/-, Rs.98, 000/-, Rs. 73,100/- and Rs.55, 400/- respectively.

Solution

Assume that r is 10%.

NPV at 10% discount rate = 18,372

Since NPV is greater than zero we have to increase discount rate, thus

NPV at 13% discount rate = 4,521

But it is still greater than zero we have to further increase the discount rate, thus

NPV at 14% discount rate = 204

NPV at 15% discount rate = (3,975)

Since NPV is fairly close to zero at 14% value of r, therefore

IRR = 14%

## REVIEW QUESTIONS

1. What is a balance sheet? Explain its components. *(R.G.P.V., Dec. 2011)*
2. What are contents of balance sheet ? *(R.G.P.V., Dec. 2010)*
3. How profit and loss accounts are prepared? *(R.G.P.V., Dec. 2012)*
4. Explain break-even point with a sketch. *(R.G.P.V., Dec. 2011)*
5. What are payback period and NPV? *(R.G.P.V., Dec. 2009)*
6. Define marketing and give its importance.
7. Explain holistic marketing concept and its components in brief.
8. What is an advertising medium? Enlist various advertising media.
9. Give procedure and objectives of marketing research.
10. Give meaning and importance of capital budgeting.

# 8 Productivity and Operations Plan

## Chapter Outline



## 8.1 INTRODUCTION

Productivity is necessary for the success of an organization. A productivity plan consists of a specific plan designed to improve efficiency. An effective productivity plan includes all areas that may affect the overall efficiency of an organization or individual. The organizational productivity plan typically addresses three main elements including:

- Operational,
- Tactical and
- Strategic planning.

Supervisor and managers may also choose to create productivity plans for individual departments or employees. The operations portion of a business plan is concerned with the day-to-day functions of running a business. Paying attention on administrative and production processes, the operations plan helps social enterprises increase efficiency and quantity, improve quality, and reduce costs. The operations plan is a good judgment of manager studies for capacity gaps that may be costing the enterprise money or service specifications.

## 8.2 MEANING AND DEFINITIONS OF PRODUCTIVITY

Productivity is the relationship between a given amount of output and the amount of input needed to produce it.

$$\text{Productivity} = \frac{\text{Outputs}}{\text{Inputs}}$$

or

Productivity = actual output/expected resources used

Productivity = value added/input of production factors

Profitability results when money is left over from sales after costs are paid. The expenditures made to ensure that the product or service meets quality specifications affect the final or overall cost of the products and/or services involved.

**Important Point:** *Productivity is defined as the ratio of what is produced to what is required to produce it. Productivity measures the relationship between output such as goods and services produced, and inputs that include labour, capital, material and other resources.*

-Hill (1993)

- *Productivity is a comparison of the physical inputs to a factory with the physical outputs from the factory.*

*-Kaplan and Cooper* (1998)

- *Productivity is the ability to satisfy the market's need for goods and services with a minimum of total resource consumption.*

*- Moseng and Rolstadas* (2001)

- *Productivity means how much and how well we produce from the resources used. If we produce more or better goods from the same resources, we increase productivity. Or if we produce the same goods from lesser resources, we also increase productivity. By "resources", we mean all human and physical resources, i.e. the people who produce the goods or provide the services, and the assets with which the people can produce the goods or provide the services.* *-Bernolak* ( 1997).

## 8.3 STANDARD OF LIVING AND HAPPINESS

The extent to which a person is able to provide the things those are necessary for sustaining and enjoying life. Standard of living of a representative family differs greatly in different parts of the world. What is considered a necessity in one part of the world could be considered a luxury in the other.

Basic necessities of a minimum decent standard of living: Food, clothing, housing and hygiene. Also, security and education are considered constituents as shown in Fig. 8.1

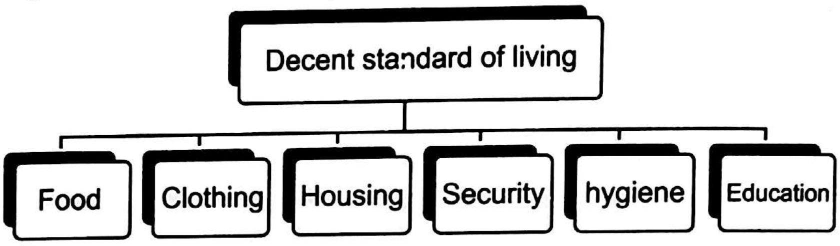


**Fig. 8.1** Decent standard of living

Greater the amount of goods and services produced in any community, the higher is the average standard of living. Standard of living generally refers to the level of wealth, comfort, material goods and necessities available to a certain socio-economic class, in a certain geographic area. An evaluation of standard of living commonly includes the following factors:

1. Income or per capita income
2. Poverty rate
3. Quality and affordability of housing
4. Cost of goods and services
5. Infrastructure
6. National economic growth

7. Economic and political stability
8. Political and religious freedom
9. Hours of work required to purchase necessities
10. Gross domestic product (GDP)
11. Inflation rate
12. Number of paid vacation days per year
13. Affordable access to quality health care
14. Quality and availability of employment
15. Class disparity
16. Quality and availability of education
17. Life expectancy
18. Incidence of disease
19. Environmental quality
20. Climate
21. Safety

## 8.4 TYPES OF PRODUCTIVITY

Productivity is one of the major concerns of managers as high productivity is essential to survive in a competitive environment. Productivity is of three types: Partial productivity, Total-factor productivity and Total productivity. The details are given below:

(i) **Partial productivity**: A measure of performance that indicates how much of a particular kind of input it takes to produce an output.

$$\text{Partial Productivity} = \frac{\text{Output}}{\text{inputs}}$$

One important input is labour productivity, which indicates the cost or number of hours of labour it takes to produce an output.

For example, labour productivity (the ratio of output to labour input) is a partial productivity measure. Similarly, capital productivity (the ratio of output to capital input) and material productivity (the ratio of output to materials input) are examples of partial productivity.

(*ii*) **Total-factor productivity:** It is the ratio of net output to the sum of associated labour and capital (factor) inputs. By "Net Output," we mean total output minus intermediate goods and services purchased. Notice that the denominator of this ratio is made up of only the labour and capital input factors.

Total-factor productivity = Net output/(Labour + Capital) input

$$\text{Total-factor productivity} = \frac{\text{(Total output - materials services purchased)}}{\text{(Labour + Capital)input}}$$

(iii) **Total productivity**: It is the ratio of total output to the sum of all input factors. Thus, a total productivity measure reflects the joint impact of all the inputs in producing the output.

Total productivity = Total output / Total input

= Total output / (human + material + capital + energy + other expenses)

We will take a simple numerical example to illustrate these three basic definitions.

Consider the ABC Company. The data for output produced and inputs consumed for a particular time period are:

| | | | | | |
|---|---|---|---|---|---|
| Output | = | 1000 | Capital Input | = | 300 |
| Human Input | = | 300 | Material Input | = | 200 |
| Energy Input | = | 100 | Other Expense Input | = | 50 |

The above values are in constant rupee terms with respect to a base period. Then, the partial, total-factor and total productivity values are computed as follows:

***Partial productivities:***

| | | | | | |
|---|---|---|---|---|---|
| Human productivity | = | Output / human input | = | 1000 / 300 = 3.33 |
| Material productivity | = | Output / material input | = | 1000 / 200 = 5.00 |
| Capital productivity | = | Output/capital input | = | 1000 / 300 = 3.33 |
| Energy productivity | = | Output/energy input | = | 1000 / 100 = 10.00 |
| Other expense productivity | = | Output/other expense input | = | 1000 / 50 = 20.00 |

***Total-factor productivity:***

Assuming that the company purchases all its materials and services, including the energy, machinery and equipment, and other services, such as marketing, advertising, information processing, consulting, etc. Then,

Net output = 1000 - ( 200 + 300 + 100 + 50 ) = 1000 - 650 = 350

Total-factor productivity = 350 / ( 300 + 300 ) = 0.583

***Total Productivity:***

= 1000 / (300 + 200 + 300 + 100 + 50 ) = 1000 / 950 = 1.053

## 8.5 OPERATIONS (GOODS AND SERVICES) VS PROJECT

In any organization, only two aspects of work exist—on-going operations and projects. The difference between operation and project management are as follows:

| *S.No.* | *Operations* | *Project* |
|---|---|---|
| 1. | Operations are ongoing execution of activities that produces the same products, or provide repetitive services.<br>Operational works are performed to achieve business goal and to sustain the business. They are permanent in nature focuses on | A project is a temporary endeavor undertaken to create a unique product, service, or result.<br>In the definition of the project, we may notice two things:<br>• A project is temporary in nature:<br>• A project is undertaken to produce a unique output; *e.g.*, |

| | | |
|---|---|---|
| | making profit for the organization. Any manufacturing or production process can be an example of operations. | product, service, or result. |
| 2. | Operational work are performed to keep organization functioning. | Projects are executed to start a new business objective and completed when it is achieved. |
| 3. | Organizations sometimes alter or modify their operations, products, or systems by creating strategic business initiatives. | Projects require project management while operations require business process management or operations management. Projects can intersect with operations at various points during the product life cycle (PLC). |
| 4. | Operations are continuing activities and permanent with recurring output. | While projects have definitive beginning and ending point. |
| 5. | Operations produce the identical product. | Projects create a unique product, service, or results. |

## 8.6 PRODUCTION PROCESSES AND LAYOUTS

Layout planning involves decisions about the physical arrangement of economic activity that facilitates various processes. Layout plans translate the broader decisions about the competitive priorities, process strategy, quality, and capacity of its processes into actual physical arrangements.

**Important Point:** *A layout essentially refers to the arranging and grouping of machines which are meant to produce goods.*

The methods of grouping or types of layout are shown in Fig. 8.2:

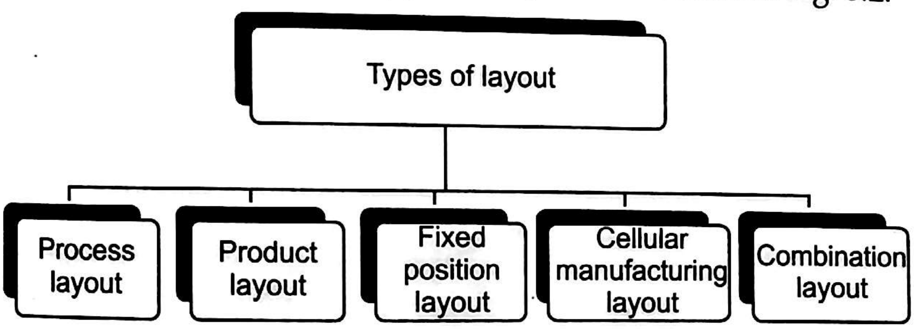


**Fig.8.2 Types of Layout**

1. **Process layout:** It involves grouping together like machines in one department based upon their operational characteristics. For example the machines performing drilling operations are installed in the drilling department while

the machines performing casting operations are grouped in casting department, and so on.

2. **Product layout:** It involves the arrangements of machines in one line, depending upon sequence of operations. In product layout, if there is a more than one line of production, there are as many lines of machines. The emphasis here, therefore, is on special purpose machines in contrast to the general purpose machines which are installed in the process layout. The investment on straight line layout is higher than in the functional layout. The product layout is followed in plants manufacturing standardized products on a mass scale such as chemical, paper, sugar, rubber, refineries and cement industries.
3. **Fixed position layout:** In a fixed position layout, workers, supplies, and equipment are brought to the site where the product are to be assembled, rather than the product being moved through an assembly line or set of assembly stations. In this type of layout, the materials or major components remains in a fixed location and tools, machinery, men and material are brought to this location. The movement of men and machines is advisable as the cost of moving them would be less significant. This is followed in manufacturing of bulky and heavy products, such as, construction of buildings, locomotives, ships, boilers, aircraft and generators.
4. **Cellular manufacturing layout (CM):** In cellular manufacturing layout, machines are grouped in to cells and these cells function somewhat like product layout within a larger shop or process layout. Each cell in the CM layout is formed to produce a single part family–a few parts all with a common characteristics, which usually means that they require the same machines and have similar machine settings.
5. **Combination layout:** A combination of process and product layout is known as combined layout. It is possible to have both types of layout in an efficiently combined form if the products manufactured are somewhat similar and not complex.

   For example in soap a plant, the machinery manufacture soap is arranged on the product line principle but ancillary services, such as heating, the manufacture of glycerin, the power house, the water treatment plant are arranged on a functional basis.

## 8.7 Inventory Management

Inventory management is a very important function that determines the health of the supply chain as well as the impacts the financial health of the balance sheet.

Any organization which is into production, trading, sale and service of a product will necessarily hold stock of various physical resources to aid in future consumption and sale. While inventory is a necessary evil of any such business, it may be noted that the organizations hold inventories for various reasons, which include speculative purposes, functional purposes, physical necessities, etc.

Inventory procurement, storage and management is associated with huge costs associated with each these functions. Inventory costs are basically categorized into three headings:

(i) Ordering Cost

(ii) Carrying Cost

(iii) Total Cost

(i) **Ordering Cost (Co):** The ordering cost is simply the total of expenses incurred in placing an order. In the economic order quantity model, this is the cost of preparing a purchase order and the cost of receiving the goods ordered used in calculating order quantities, the costs that increase as the number of orders placed increases. It includes costs related to the clerical work of preparing, releasing, monitoring, and receiving orders, the physical handling of goods, inspections, and setup costs, as applicable also called acquisition cost, inventory costs.

(ii) **Carrying Cost or Holding Cost (Cc):** The holding cost, on the other hand, is the cost associated with holding one unit of an item in stock for one period of time incorporating elements to cover: Capital costs for stock, taxes, insurance, storage, handling, administration, shrinkage, obsolescence, deterioration. In business management, holding cost is money spent to keep and maintain a stock of goods in storage.

(iii) **Total Cost (TC):** It is the sum of ordering cost and carrying cost (holding cost).

**Thus total cost is:**

**Total Cost (TC) = Ordering Cost (Co)+ Carrying Cost (Cc)**

## 8.8 Economic order Quantity (EOQ)

Economic order quantity is one of the techniques of inventory control which minimizes total carrying costs and ordering costs for the year. The economic order quantity is the technique which solves the problem of the materials manager. EOQ involves determining the optimal quantity to purchase when orders are placed. For example, small orders result in low inventory carrying costs and higher ordering costs; while large orders result in low ordering costs and high carrying costs.

**Important Point:** *"EOQ is essentially an accounting formula that determines at which the combination of order costs and inventory carrying cost are the least. The result is the most cost effective quality to order. In purchasing this is known as order quantity, in manufacturing it is known as the production lot size."* *-Dave Piasecki*

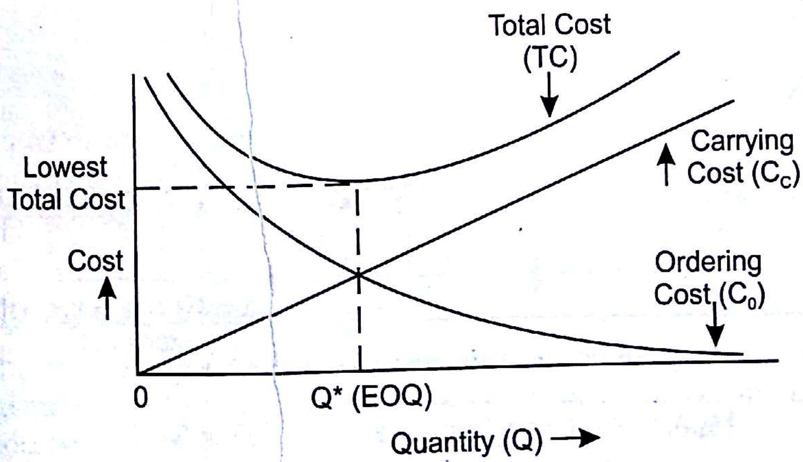


**Fig.8.3** Economic order Quantity

There is a pre-determined cost charged for each order sited, not consideri of the number of units ordered. There is also a carrying or holding or store-roo cost for each unit held in luggage compartment. The optimal number of units the inventory is to order so that we reduce the total cost related with the delive purchase, and storage of the manufactured goods as shown in Fig. 8.3.

Thus,

**Economic Order Quantity (EOQ)→ Ordering Cost (Co) = Carrying Cost (C**

**[Total Cost (TC) is lowest or minimum at this point]**

The necessary parameters to the resolution are the total order for the year, th procure cost for each item, the fixed cost to place the order and the storage charge for each piece per year. Note that the quantity of times an order is located wil also have an effect on the total cost, however, this number can be determined from the other parameters.

Mathematical model that determines the amount of goods to order to meet projected demand while minimizing inventory costs. In the original version of the model, demand is assumed to be known and constant throughout the year. Ordering cost is assumed to be a fixed amount per order, and carrying costs are assumed to be constant per unit. EOQ is computed as:

$$\text{ECQ} = \sqrt{\frac{2(\text{Annual Demand})\ (\text{Ordering Cost})}{\text{Carrying Cost Per Unit}}}$$

***Basic Assumptions of EOQ Model:***

EOQ is one of the most common known inventory control technique. This technique involves some assumptions:

1. Demand is known and constant.
2. The lead time is known and constant.
3. The receipt of inventory is instantaneous.
4. Quantity discounts are not possible.
5. The only variable costs are the ordering cost and the carrying cost.
6. Orders are placed so that stock-outs are avoided.

***Re- Order Point and Buffer/ Safety Stock:***

The re-order point (ROP) is the level of inventory when an order should be made with suppliers to bring the inventory up by the Economic order quantity ("EOQ") as shown in Fig. 8.4.

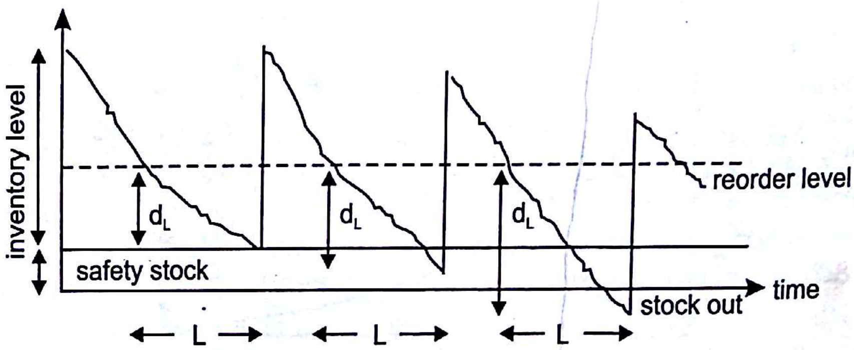


**Fig.8.4 Re- Order Point and Buffer/ Safety Stock**

The following two formulae are used for the calculation of re-order level or point.

**Ordering point = Maximum usage (daily or weekly or monthly) × Lead time (L)**

The above formula is used when usage and lead time are known with certainty; therefore, no safety stock is provided.

When safety stock is provided then the following formula will be applicable:

**Ordering point = [Maximum usage (daily or weekly or monthly) × Lead time] + Safety stock**

## 8.9 ABC-Analysis

ABC analysis classifies the raw materials based on their consumption during a particular time period (usually one year). Depending upon the company to company A, B and C items can be as under and also shown in Fig. 8.5:

- A - Approx 5% - 10% of the items accounting for 60% to 80% of the consumption value.
- B - Approx 10 %-30% of the Items accounting for 10% to 30% of the consumption value.
- C -Approx 60%-85% of the Items accounting for 5% to 15% of the consumption value.

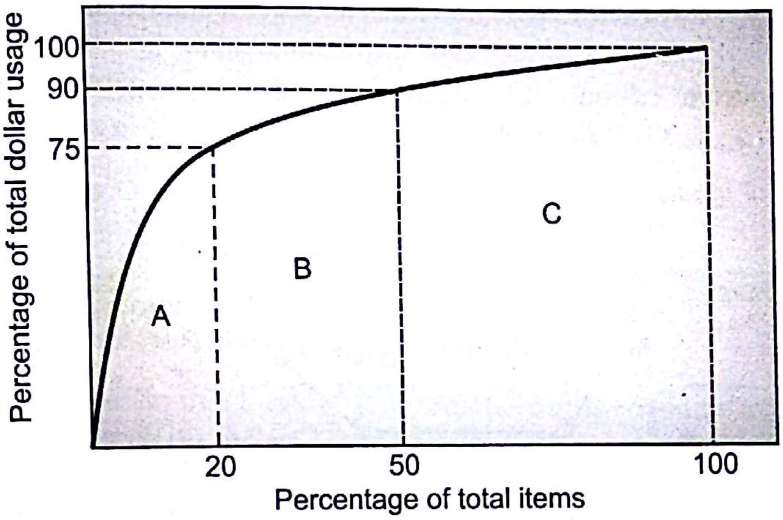


Fig.8.5 ABC -Analysis

Similar or the same as ABC analysis is 80/20 rule that is also known as Pareto Principle. This rule tells us that 80% of effects are due to 20% of causes, in other words we can say that 80% of our sáles comes from 20% of our customers.

## 8.10 XYZ-Analysis

XYZ analysis is similar to ABC but concentrates on inventory to improve storage management and it is more used in relation of the customer demand for finished commodities. These three types of products are as follows:

- X is high demand products.
- Y is medium demand products.
- Z is very low demand products.

ABC/XYZ analysis is used to generate the strategic for the supply and inventory control and production strategy.

## 8.11 MATERIAL REQUIREMENT PLANNING (MRP)

Material requirements planning (MRP) is a computer-based production planning and inventory control system. MRP is concerned with both production scheduling and inventory control. It is a material control system that attempts to keep adequate inventory levels to assure that required materials are available when needed. MRP is applicable in situations of multiple items with complex bills of materials.

**Important Point:** *MRP is a production planning process that starts from the demand for finished products and plans the production step by step of sub-assemblies and parts.*

The major objectives of an MRP system are simultaneously to:

1. Ensure the availability of materials, components, and products for planned production and for customer delivery,
2. Maintain the lowest possible level of inventory and reduces holding costs,
3. Plan manufacturing activities, delivery schedules and purchasing activities.

The component of material requirement planning (MRP) are:- MRP Inputs, MRP Processing as MRP Outputs as shown in following Fig. 8.6.

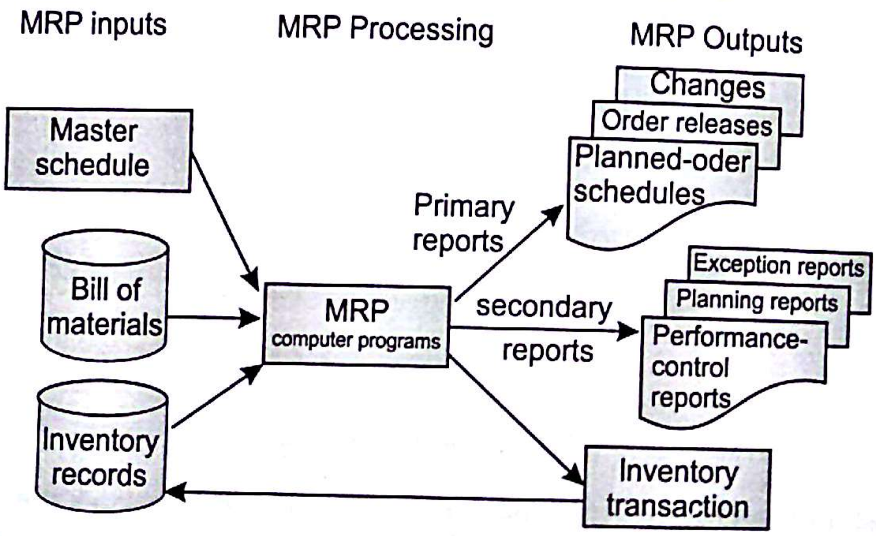


**Fig. 8.6** Component of Material Requirement Planning (MRP)

1. **MRP Inputs:** The input systems come from three main sources:
   (i) **Master schedule.** The master schedule outlines the expected production activities of the plant. Developed using both internal forecasts and external orders, it states the quantity of each product that will be manufactured and the time frame in which they will be needed.
   (ii) **Bill of materials.** The bill of materials is a listing of all the raw materials,

component parts, sub-assemblies, and assemblies required to produce one unit of a specific finished product. Each different product made by a given manufacturer will have its own separate bill of materials.

(iii) **Inventory records.** The inventory records file provides an accounting of how much inventory is already in-hand or on order, and thus should be subtracted from the material requirements. This includes gross requirements, scheduled receipts, and expected amount in- hand. It also includes other details for each item, such as supplier, lead time, and lot size.

2. **MRP Processing**: MRP processing first determines gross material requirements, then subtracts out the inventory in- hand and adds back in the safety stock or buffer stock in order to compute the net requirements.
3. **MRP Output**: The main outputs from MRP include three primary reports and three secondary reports.

(i) **Primary Report.** The primary reports consist of:

*(a)* **Planned order schedules**: These outline the quantity and timing of future material orders.

*(b)* **Order releases**: It authorizes orders to be made; and

*(c)* **Changes to planned orders**: These might include cancellations or revisions of the quantity or time frame.

(ii) **Secondary reports**: It generated by MRP include:

*(a)* **Performance control reports**: Which are used to track problems like missed delivery dates and stock outs in order to evaluate system performance.

*(b)* **Planning reports**: These reports can be used in forecasting future inventory requirements.

*(c)* **Exception reports**: These reports call managers' attention to major problems like late orders or excessive scrap rates.

## 8.12 SUPPLY CHAIN MANAGEMENT (SCM)

The term "supply chain management" entered the public domain when **Keith Oliver**, a consultant at Booz Allen Hamilton, used it in an interview for the Financial Times in 1982. *Supply Chain Management is popularly known as SCM or sometimes referred to as Demand Chain Management or DCM.*

### 8.12.1 Meaning & Definitions

A supply chain is a system of facilities and distribution selections that executes the functions of procurement of materials, transformation of these materials into intermediate and finished products, and the distribution of these finished products to customers and/or consumers (end users) as shown in Fig.8.7. Supply chain exists in both service and manufacturing organizations, although the complexity of the chain may vary greatly from organization to organization.

Thus, Supply Chain Management (SCM) is the management of the entire value-added chain, from the supplier to manufacturer right through to the retailer and the final customer.

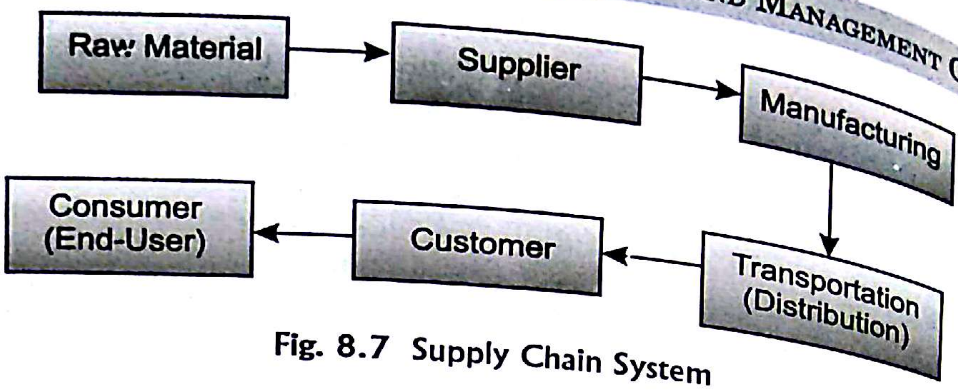


**Fig. 8.7 Supply Chain System**

**Important Point:** *"A supply chain is the link between raw materials and the end-user creating a flow of goods, information, and funds. It not only includes the company, but also its suppliers, buyers, vendors, customers, and others with whom it interacts."*

- *"Supply Chain Management (SCM) has three primary goals: Reduce inventory, increase the transaction speed by exchanging data in real-time, and increase sales by implementing customer requirements more efficiently."*
- *"Supply Chain Management is the integration of key business processes across the supply chain for the purpose of creating value for customers and stakeholders." Lambert, 2008.*
- *"Supply chain management is the systematic, strategic coordination of the traditional business functions and the tactics across these business functions within a particular company and across businesses within the supply chain, for the purposes of improving the long-term performance of the individual companies and the supply chain as a whole."* - Mentzer et al., 2001

A very simple supply chain for a single product, where raw material is procured from vendors, transformed into finished goods in a single step, and then transported to distribution centers, and finally, customers. Realistic supply chains have numerous end products with shared components, facilities and capacities. The flow of materials is not always along an arborescent network, various modes of transportation may be considered.

## 8.12.2 Supply Chain Decisions

The decisions for supply chain management has been classified into two broad categories –

**Strategic.** Strategic decisions are made typically over a longer time horizon. These are closely linked to the corporate strategy, and guide supply chain policies from a design perspective.

**Operational.** These are short term decisions that focus on activities over a day-to-day basis. The effort in these types of decisions is to effectively and efficiently manage the product flow in the "strategically" planned supply chain.

There are four major decision areas in supply chain management:

(a) **Location.** The geographic placement of production facilities, stocking points, and sourcing points is the natural first step in creating a supply chain.

(b) **Production.** The strategic decisions include what products to produce, which plants to produce them in and allocation of suppliers to plants.

(c) **Inventory.** Inventories exist at every stage of the supply chain as either

raw material, semi-finished or finished goods. Their primary purpose to buffer against any uncertainty that might exist in the supply chain.

(d) **Transportation (Distribution).** These are closely linked to the inventory decisions, since the best choice of mode is often found by trading-off the cost of using the particular mode of transport with the indirect cost of inventory associated with that mode. There are both strategic and operational elements in each of these decision areas.

### 8.12.3 SCM Solution

There are four dimensions to an integrated SCM Solution:

1. Integration of purchasing, manufacturing, transportation and warehousing activities.
2. Integration of above activities across vendors, facilities, and markets.
3. Integration of these activities over strategic, tactical and operational planning.
4. Enterprise wide integration.

### 8.12.4 Benefits of SCM Solution

The SCM solution has several benefits as companies can forecast:

- Production planning
- Flow and process management
- Inventory management
- Customer delivery
- After-sales support and service
- Shipment tracking systems

# 9 Productivity: Method Improvement and Models

## Chapter Outline

- Steps in Method Improvement
- Time Measurement
- Rating and Various Allowances
- Predetermined Motion and Time Method
- Product and Process Specification
- Total Quality Management (TQM)
- Cost of Quality
- Introduction to Lean Manufacturing –Just-in-Time (JIT)
- Quality Function Deployment (QFD)
- Total Productive Maintenance (TPM)
- Six Sigma Quality (6σ)
- Enterprise Resource Planning (ERP)

## 9.1 STEPS IN METHOD IMPROVEMENT

A continual improvement is a type of change that is focused on increasing the effectiveness and efficiency of an organization to fulfill its policies and objectives. It is not limited to quality initiatives. Improvement in business strategy, business results, customer, employee, and supplier business relationships are subject to continual enhancement. Steps to undertaking continual improvement are as follows:

1. Determine current performance.
2. Establish a need to improve.
3. Obtain commitment and define the improvement objective.
4. Organize the diagnostic resources.
5. Carry out research and analysis to discover the cause of current performance.
6. Define and test solutions that will accomplish the improvement objective.
7. Produce improvement plans which specify how and by whom the alteration will be implemented.
8. Identify and overcome any resistance to the change.
9. Implement the change.
10. Put in place and control to hold new levels of performance, and repeat step one.

## 9.2 TIME MEASUREMENT

A work measurement technique whereby times established for basic human motions classified according to the nature of the motion and conditions (under which it is made) are used to build up the time for a job at the defined level of performance.

**Important Point:** *Time measurement is the determination of length of time one should take to complete a job.*

The most commonly used Pre-determined Motion Time System (PMTS) is known as Methods Time Measurement (MTM).

## 9.3 RATING AND VARIOUS ALLOWANCES

Employers must take this non-productive time into consideration when determining piece rates by including what is known as a **Personal, Fatigue, and Delay (PF&D) factor.** Allowances are generally applied to total cycle time as some percentage of it, but sometimes these are given separately as some percent for machine time and for manual effort time. However, no allowances are given for interruptions which may be due to factors which are within the operator's control or which are avoidable. In US, generally, not less than 15% allowances (9 - 10 minutes per hour) shall be used in conducting time studies." Most companies allow the following allowances to their employees as shown in Fig. 9.1.

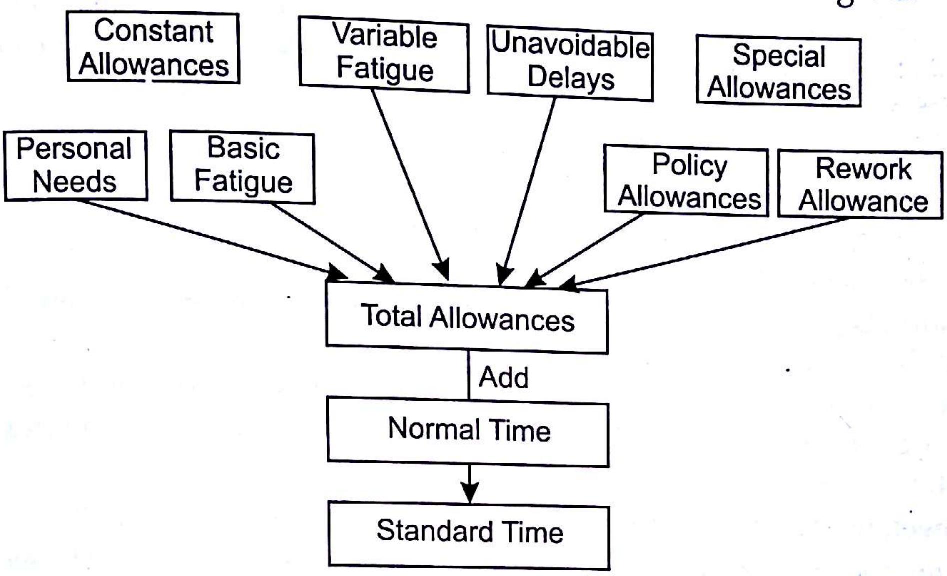


**Fig. 9.1** Allowances to employees

(i) **Delay Allowance:** This time allowance is given to operator for the numerous unavoidable delays and interruptions that he experiences every day during the course of his work. These interruptions include interruptions from the supervisor, inspector, planners, expediters, fellow workers, production personnel and others.

(ii) **Fatigue Allowance:** This allowance can be divided into two parts: (i) basic fatigue allowance and (ii) variable fatigue allowance. The basic fatigue allowance is given to the operator to compensate for the energy expended for carrying out the work and to alleviate monotony. While the magnitude of variable fatigue allowance given to the operator depends upon the severity of conditions, which cause extra (more than normal) fatigue to him. As we know, fatigue is not identical.

(iii) **Personal Allowance:** This is allowed to compensate for the time spent by worker in meeting the physical needs, for instance a periodic break in the production routine.

(iv) **Special Allowances:** These allowances are given under certain special circumstances. Some of these allowances and the conditions under which they are given are:

(a) **Policy Allowance:** Some companies, as a policy, give an allowance to provide a satisfactory level of earnings for a specified level of performance under exceptional circumstance. This may be allowed to new employees, handicap employees, workers on night shift, etc. The value of the allowance is typically decided by management.

(b) **Rework Allowance:** This allowance is provided on certain operation when it is known that some percent of parts made are spoiled due to factors beyond the operator's control. The time in which these spoiled parts may be reworked is converted into allowance.

## 9.4 PREDETERMINED MOTION AND TIME METHOD

A pre-determined motion time system method or system (PMTS) may be defined as a procedure that analyzes any manual activity in terms of basic or fundamental motions required to perform it. Each of these motions is assigned a previously established standard time value and then the timings for the individual motions are synthesized to obtain the total time needed for performing the activity. The applications of PMTS are for:

- Determination of job time standards.
- Comparing the times for alternative proposed methods so as to find the economics of the proposals prior to production run.
- Estimation of manpower, equipment and space requirements prior to setting up the facilities and start of production.
- Developing tentative work layouts for assembly lines prior to their working in order to minimize the amount of subsequent re-arrangement and rebalancing.
- Checking direct time study results.
- A number of pmts are in use, some of which have been developed by individual organizations for their own use, while other organizations have developed and publicized for universal applications.

## 9.5 PRODUCT AND PROCESS SPECIFICATION

The term 'specification' means– with the type of process, information, or document.

(i) **Specification process:** It is an inherent part of the design process; it consists of determining and communicating the nature and quality (as distinct from geometry, size and shape) of each element, system, type of work, product, etc.

(ii) **Specification information:** It is written and numeric description resulting from the specification process.

(iii) **Specification document:** A document consisting principally of specification information.

### 9.5.1 Production specification

Production specification should define the quality of the systems, products, workmanship and finished work such that all parties can have a reasonable degree of confidence that:

- The designers' detailed requirements will be met.
- The work can be priced with certainty and accuracy.
- Products can be ordered or arranged correctly and in good time.
- The work can be planned, executed and supervised in a controlled manner.
- Misunderstandings and unintended variations are minimized.

### 9.5.2 Attributes of good production specification

Production specification should be:

1. Specific to the project, with no irrelevant material.
2. Comprehensive covering, *i.e.*, every significant aspect of quality to a degree of detail appropriate to the importance and nature of the work.
3. Practicable, requirements being specified having regard to the nature of the project and the available knowledge and resources.
4. Constructive, in other words helpfully specific, so that all parties know what is expected.
5. Technically correct and up to date, reflecting current good building practice and current statutory requirements.
6. Enforceable, requirements being specified only if compliance can be demonstrated economically and within an acceptable timescale.
7. Well co-ordinated, with no conflicts or ambiguities, either within itself or with drawings and measured information.
8. Developed throughout the project lifecycle, to become an essential part of information.

### 9.5.3 Process Specification

The term process specification refers to a description of the procedure to be followed by an actor within an elementary level business activity, as represented on a process model such as a dataflow diagram. Process specification is a generic term for the specification of a process. Its context is not unique to "business activity" but can be applied to any organizational activity.

**Important Point:** *The process specification defines what must be done in order to transform inputs into outputs. It is a detailed set of instructions outlining a business procedure that each elementary level business activity is expected to carry out. Process specifications are commonly included as an integral component of a requirements document in systems development.*

The goals of producing process specifications are:

- To reduce process haziness.
- To obtain a precise description of what is accomplished.
- To validate the system design, including data flow diagrams and the data dictionary.

## 9.6 Total Quality Management (TQM)

Total quality management is a common sense dedication to understanding what the customer wants and then using people and science to set up systems to deliver

products and services that delight the customer. All of the TQM model's elements are working together to achieve results.

The basic concepts of TQM are as follows:

- Customer Focus.
- Continuous Process Improvement.
- Employee Empowerment – Everyone is responsible for quality.
- Quality is free - focus on defect prevention rather than defect detection for it is always cheaper to do it right the first time.
- Benchmarking – Legally stealing or copying other people's ideas.
- Customer-Supplier Partnerships.
- Management by fact, By numbers, By data – Balanced scoreboard (financial, customer, process, learning.

TQM requires a new process thinking mindset. Our focus shifts from managing outcomes to managing and improving processes from what to do to how to do the processes better. Quality performance expands to include how well each part of the process works and the relationship of each part to the process. It is also the process improvement that focuses on continuously benefit for our customers. The following Fig. 9.2 shows the elements of TQM Model:

1. **Customer focus**: The model begins with understanding customer needs. TQM organizations have processes that continuously collect, analyze, and act on customer information to satisfy their needs and wants.
2. **Planning and process management**: TQM organizations understand that customers will only be satisfied if they consistently receive products and services that meet their needs, are delivered when expected, and are priced for value. TQM organizations use the techniques of process management to develop cost-controlled processes that are stable and capable of meeting customer expectations.
3. **Process improvement**: TQM organizations also understand that exceptional performance today may be unacceptable performance in the future so they use the concepts of process improvement to achieve both breakthrough gains and incremental continuous improvement.

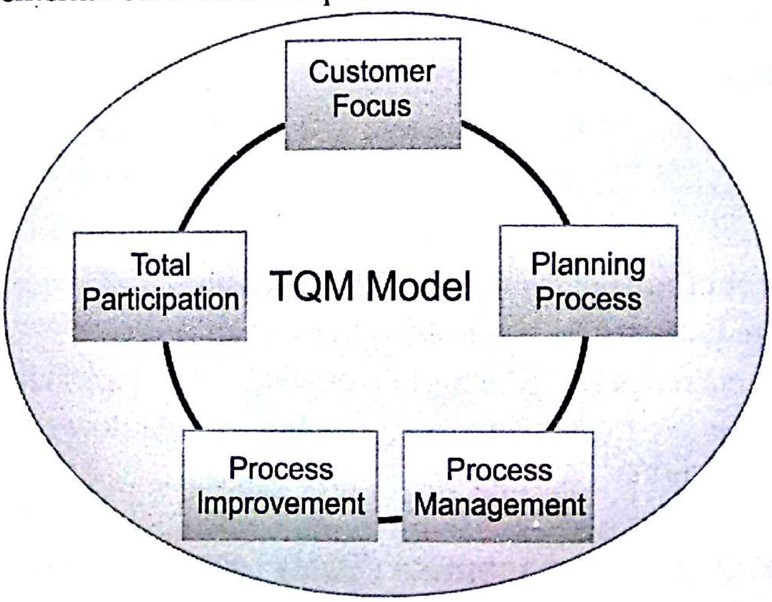


**Fig. 9.2** Elements of TQM Model

4. **Total participation:** The final element of the TQM model is total participation. TQM organizations understand that all work is performed through people. This begins with leadership.

There are seven basic quality tools which help to improve process quality:

1. **Scatter Diagrams:** Plot data on a chart – no attempt is made to classify the data or message it.
2. **Pareto Charts:** Organize data on a histogram based on frequency from most prevalent to least. Help identify major causes or occurrences (80:20 rules).
3. **Check Sheets:** It is an easy way to count frequency of occurrence by front line workers.
4. **Histograms:** It categorizes data in cells and plots (see if any patterns emerge).
5. **Run Charts:** Plot data as a function of time.
6. **Cause and effects Charts:** Fishbone diagrams are used to identify the root causes of a problem.
7. **Control Charts:** These are statistical tools used to determine if the variation in results is caused by common or special events.

## 9.7 COST OF QUALITY

The cost of quality refers to the sum of costs incurred to prevent non-conformance from happening and the costs incurred when non-conformance in products and system occurs. This is commonly known as cost of poor quality. Cost of poor quality is actually the cost of doing things wrong. Cost of poor quality refers to the costs associated with providing poor quality product or service. Cost of quality fall into two main categories:

1. Cost of achieving good quality -Prevention Costs Appraisal Costs
2. Cost of poor quality due to internal failure and/or external failure.

## 9.8 INTRODUCTION TO LEAN MANUFACTURING – JUST-IN-TIME (JIT)

The basic elements of JIT were developed by **Toyota** in the 1950's, and became known as the Toyota Production System (TPS). JIT was well-established in many **Japanese factories** by the early 1970's. JIT began to be adopted in the U.S. in the 1980's (General Electric was an early adopter), and the JIT/lean concepts are now widely accepted and used.

Just in time (JIT) is a production strategy that strives to improve a business return on investment by reducing in-process inventory and associated carrying costs.

Just in time manufacturing (JIT) is one of the main principles of lean manufacturing or stockless production. It is the idea of producing exactly what the customer wants, in the quantities they want, where they want it, when the customer wants it without being delayed or held up in inventory. JIT (also known as lean production or stockless production) should improve profits and return on investment by reducing inventory levels (increasing the inventory turnover rate),

reducing variability, improving product quality, reducing production and delivery lead times, and reducing other costs (such as those associated with machine setup and equipment breakdown). In a JIT system, underutilized (excess) capacity is used instead of buffer inventories to hedge against problems that may arise.

JIT tries to reduce the system operational inefficiencies and the resulting waste by identifying the sources of these inefficiencies and working proactively to eliminate them as much as possible. In the emerging philosophy, inventories should be carefully controlled and they should not function as the mechanism for accommodating the system inefficiencies→Just-in-Time (JIT). The aforementioned effort should be an ongoing process towards continuous improvement rather than one-time/shot effort. Targeting the sources of inefficiency includes:

1. **Input**
   - Unreliable quality of raw material
   - Unreliable delivery times
2. **Operation**
   - Unreliable processes in terms of
   - Required processing times
   - Process outcome
   - Complex interacting process flows
   - Long set-up times
   - Unreliable (irresponsive and irresponsible) personnel
3. **Output**
   - Highly variable production requirements in terms of
   - production volume, and
   - production scope

**JIT Implementation Design.** Based on a diagram modeled after the one used by Hewlett-Packard's Boise plant to accomplish its JIT program.

1. **F Design Flow Process**
   - F Redesign/re-layout for flow
   - L Reduce lot sizes
   - O Link operations
   - W Balance workstation capacity
   - M Preventive maintenance
   - S Reduce setup times
2. **Q Total Quality Control**
   - C Worker compliance
   - I Automatic inspection
   - M Quality measures
   - M Fail-safe methods
   - W Worker participation
3. **S Stabilize Schedule**
   - S Level schedule
   - W Establish freeze windows

- UC Underutilize capacity

4. K **Kanban Pull System**
   - D Demand pull
   - B Back flush
   - L Reduce lot sizes
5. V **Work with Vendors**
   - L Reduce lead time
   - D Frequent deliveries
   - U Project usage requirements
   - Q Quality expectations
6. I **Further Reduce Inventory in other areas**
   - S Stores
   - T Transit
   - C Implement carrousel to reduce motion waste
   - C Implement conveyor belts to reduce motion waste
7. P **Improve Product Design**
   - P Standard production configuration
   - P Standardize and reduce the number of parts
   - P Process design with product design
   - Q Quality expectations

## 9.9 QUALITY FUNCTION DEPLOYMENT (QFD)

Quality function deployment (QFD) was developed to bring this personal interface to modern manufacturing and business. In today's industrial society, where the growing distance between producers and users is a concern, QFD links the needs of the customer (end user) with design, development, engineering, manufacturing, and service functions.

**Important Point:** *Quality function deployment (QFD) is a structured approach of defining customer needs or requirements and translating them into specific plans to produce products to meet those needs.*

The "voice of the customer" is the term to describe these stated and unstated customer needs or requirements. The voice of the customer is captured in a variety of ways: direct discussion or interviews, surveys, focus groups, customer specifications, observations, warranty data, field reports, etc. This understanding of the customer needs is then summarized in a product planning matrix or "House of Quality" as shown in Fig. 9.3.

To build a house of quality the following aspects are to be considered:

- List Customer Requirements (What's)
- List Technical Descriptors (How's)
- Develop Relationship (What's & How's)
- Develop Inter-relationship (How's)
- Competitive Assessments

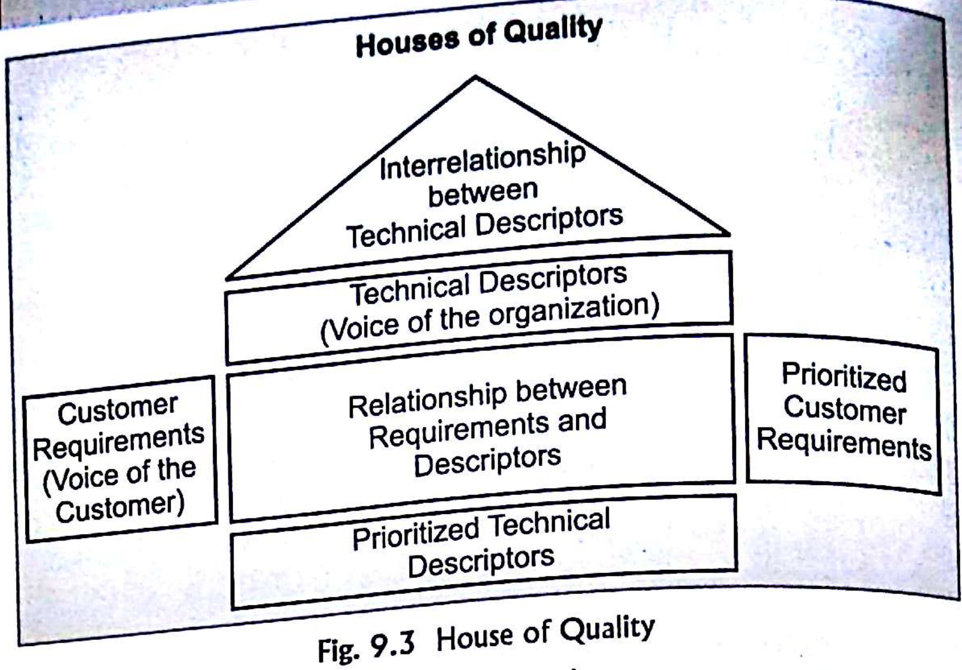


Fig. 9.3 House of Quality

- Prioritize Customer Requirements
- Prioritize Technical Descriptors

**QFD Matrix.** These matrices are used to translate higher level "what's" or needs into lower level "how's" - product requirements or technical characteristics to satisfy these needs as shown in the Fig. 9.4.

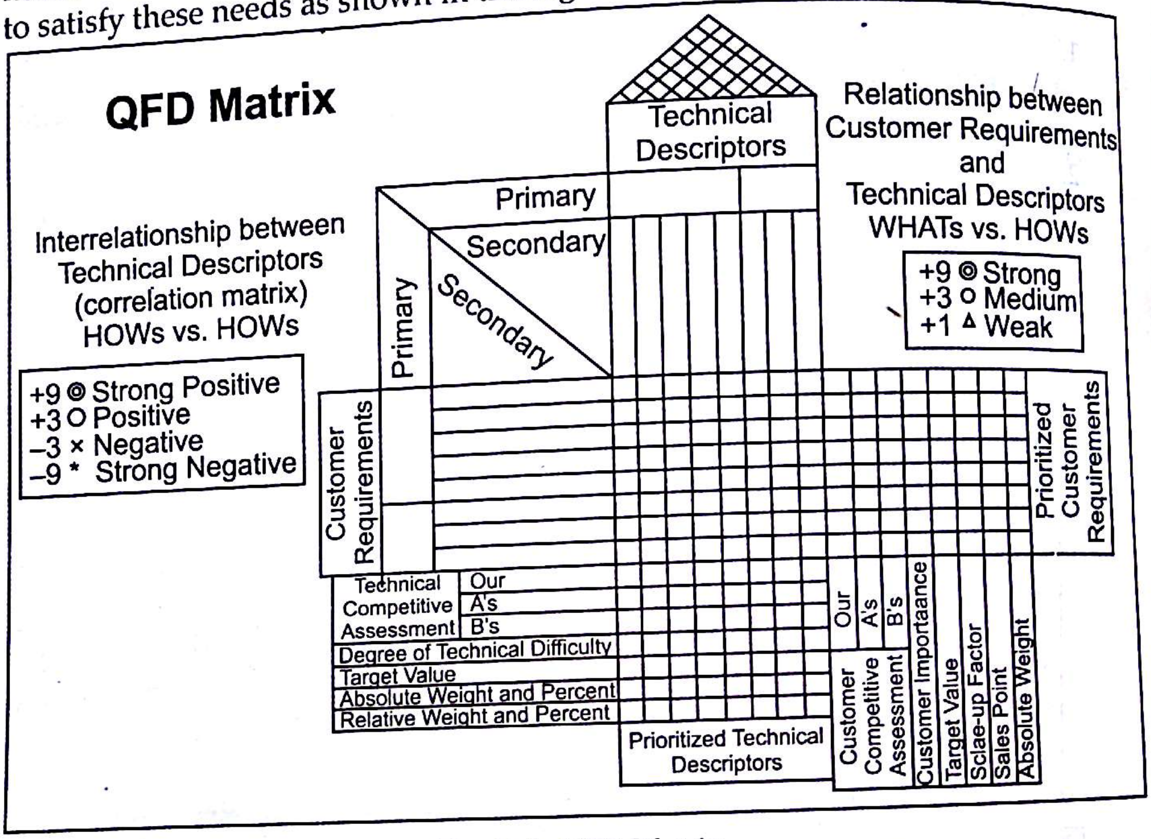


Fig. 9.4 QFD Matrix

## 9.10 TOTAL PRODUCTIVE MAINTENANCE (TPM)

Total productive maintenance (TPM) is a fundamental change in the entire organization, which focuses everyone towards improved equipment effectiveness.

TPM is not a short-term fix, but a long, everlasting journey to best in class factory performance through:

- On-going management commitment
- Increased employee responsibilities
- Cross-functional teams
- Root cause fixes
- Discipline, standardization and simplification
- Continuous improvement

**Important Point:** *Total productive maintenance (TPM) is a maintenance program which involves a newly defined concept for maintaining plants and equipment. The goal of the TPM program is to markedly increase production while, at the same time, increasing employee morale and job satisfaction.*

TPM was introduced to achieve the certain objectives. The important ones are listed below:

1. Avoid wastage in a quickly changing economic environment.
2. Producing goods without reducing product quality.
3. Reduce cost.
4. Produce a low batch quantity at the earliest possible time.
5. Goods send to the customers must be non-defective.

**Pillars of TPM:** The eight pillars of TPM are shown in Fig. 9.5.

1. **Autonomous Maintenance:** Maintenance is performed by the machine operator rather than the maintenance staff. Autonomous maintenance includes tasks such as: lubricating and tightening machine parts.
2. **Focused Improvement:** Focused Improvement is the process of applying systematic problem solving methods to manufacturing. The process relies on aligning the correct method to the correct scenario.

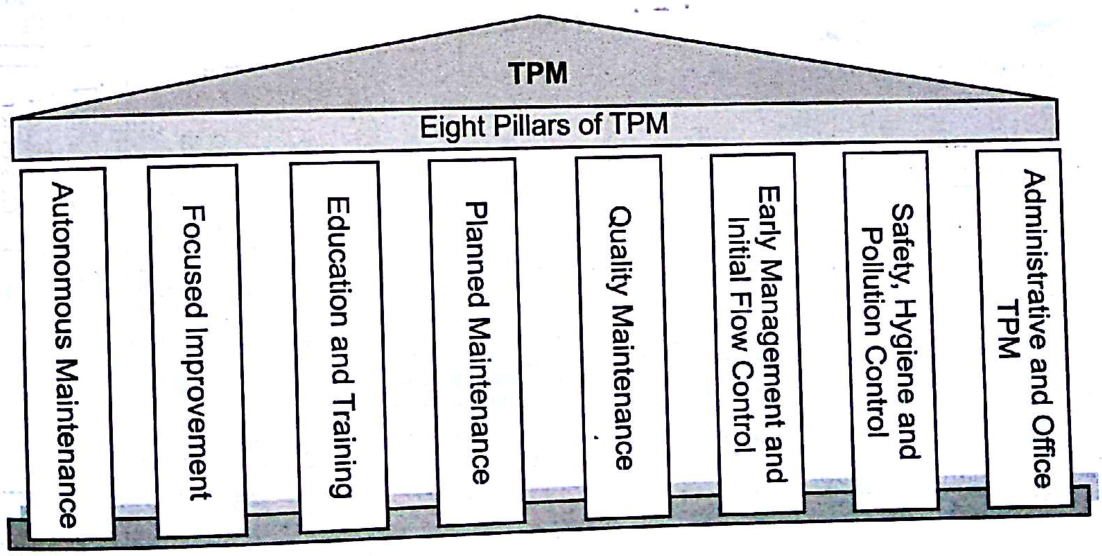


**Fig. 9.5** Pillars of TPM

3. **Education and Training:** It is aimed to have multi-skilled re-energized employees whose morale is high and who has eager to come to work and perform all required functions effectively, efficiently and independently. Education is given to operators to upgrade their skill. It is not sufficient to know only "Know-How" by they should also learn "Know-why". The employees should be trained to achieve the all phases of skill. The goal is to create a factory full of experts.
4. **Planned Maintenance:** Schedules maintenance tasks based on predicted and/or measured failure rates.
5. **Quality Maintenance:** Design error detection and prevention into production processes. Apply root cause analysis to eradicate recurring sources of quality defects.
6. **Early Management and Initial Flow Control:** It directs practical knowledge and understanding of manufacturing equipment gained through TPM towards improving the design of new equipment. The small group of employees work together is proactively to achieve regular, incremental improvements in equipment operation.
7. **Safety, Hygiene and Pollution Control:** Maintain a safe and healthy working environment.
8. **Administrative and Office TPM:** Apply TPM techniques to administrative functions.

## 9.11 SIX SIGMA QUALITY (6σ)

The term six sigma originated from terminology associated with manufacturing, specifically terms associated with statistical modeling of manufacturing processes. Six sigma (6σ) is a process improvement set of tools and strategies, originally developed by **Motorola in 1986**. Sigma is a measure of "goodness: the capability of a process to produce perfect work". A defect is any mistake that results in customer dissatisfaction.

**Important Point:** *Six sigma seeks to improve the quality of process outputs by identifying and removing the causes of defects (errors) and minimizing variability in manufacturing and business processes.*

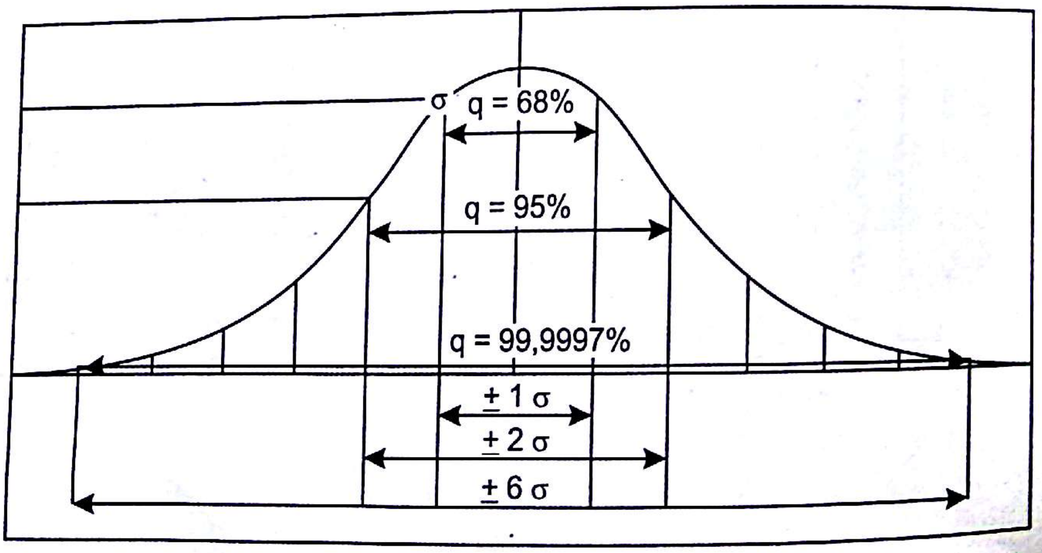


**Fig.9.6** Six Sigma measures defects based around the statistical methods

Sigma indicates how often defects are likely to occur, as shown in Fig. 9.6, a six sigma process is one in which 99.99966% of the products manufactured are statistically expected to be free of defects (3.4 defects per million). The higher the sigma level, the lower the defect rate. The lower the defect rate, the higher the quality.

The maturity of a manufacturing process can be described by a sigma rating indicating its yield or the percentage of defect-free products it creates.

***Six Sigma Roles:***

Sigma also defines five specific roles for successful implementation. These are:

- Executive Leader
- Champions
- Master Black Belts
- Black Belts
- Green Belts.

Specific training courses are widely available to support these roles.

### 9.11.1 Six Sigma Processes

There are two six sigma processes:

- Six Sigma DMAIC
- Six Sigma DMADV

Each term derived from the major steps in the process.

1. **DMAIC.** DMAIC is divided into five separate phases. They are Define, Measure, Analyze, Improve, and Control as shown in Fig. 9.7. The meaning or how the method is implemented is as follows:

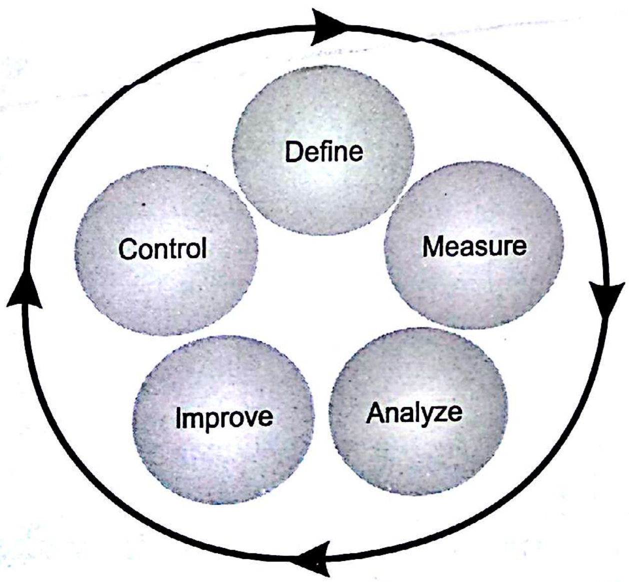


**Fig. 9.7 Six Sigma DMAIC**

(i) **Define:** The means to define high level and priority project goals and the process needed to achieve them. If there is a problem in the process, six sigma supervisors must define the problem clearly in order to fix it.

(ii) **Measure:** The key aspects and characteristics of a process should be measured and collect relevant and reliable data. This includes assembling the data into a plan, executing the plan, and making sure that the data was collected properly.

(iii) **Analyze:** After everything has been measured, the data that is collected should be analyzed to determine the cause-and-effect relationship of the process in question. The analysis stage is often done by a Six Sigma Black Belt. By using the collected data, the Black Belt will come up with a hypothesis on the cause of the problem in the process. By using statistical tools, the hypothesis will be tested.

(iv) **Improve:** After the data has been analyzed, a solution should be reached to improve the process. This stage is also completed by a Black Belt.

(v) **Control:** The process needs to be controlled to ensure that all variables that lead to defects are corrected. The process should also be monitored continuously to watch out for recurring defects. Any process can be affected by a number of factors, no matter how small. By continually monitoring the process, operators can watch for variables that might occur and correct them before they can cause further defects.

2. **DMADV**—Six Sigma DMADV is also divided into five separate phases. They are defines measures, analyzes, designs, and verifies new processes or products that are trying to achieve six sigma quality as shown in Fig. 9.8.

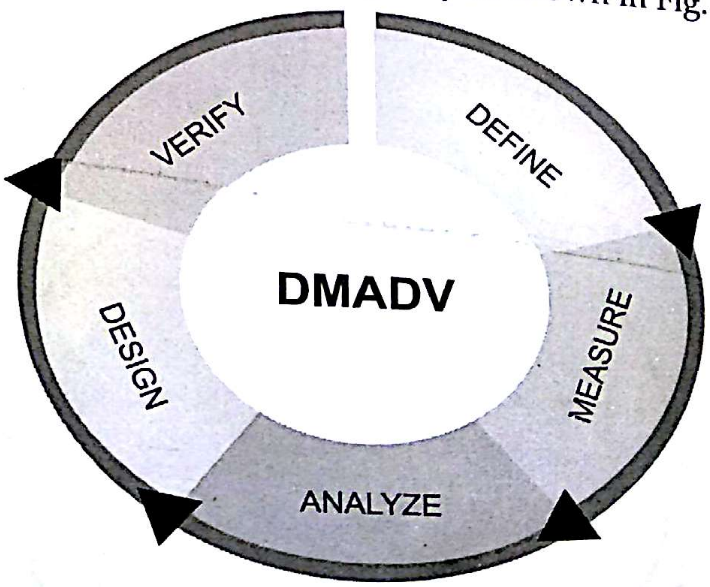


**Fig. 9.8** Six Sigma DMADV

(i) **Define:** This stage is supposed to set the project goals that are needed to meet customer demand, satisfaction, and the overall strategy of the company.

(ii) **Measure:** This is used to identify the aspects that are important to Critical-to-Quality, process capabilities, customer satisfaction, and risks of the project in question.

(iii) **Analyze.** Data must be analyzed to develop alternative designs as well as evaluate certain design capabilities and select the most appropriate design. By analyzing the various alternative processes, it is easier to achieve customer satisfaction.

(iv) **Design.** In this stage six sigma team members will optimize a design to get the most out of it. This involves design modifications, alterations, and verification. The goal is to make the best possible to meet customer needs and wants.

(v) **Verify.** This stage makes sure the design works to perfection by setting up trial runs and finally implementing it into full production. Six Sigma team members monitor the new design before handing it back to the regular process operators.

### 9.11.2 Difference between DMAIC and DMADV

| S. No. | DMAIC (Define, Measure, Analyze, Improve, and Control) | DMADV (Defines, Measures, Analyzes, Designs, and Verifies) |
|---|---|---|
| 1. | DMAIC is divided into five separate phases. They are Define, Measure, Analyze, Improve, and Control. | The five phases of DMADV are : Defines, Measures, Analyzes, Designs, and Verifies new processes or products that are trying to achieve six sigma quality. |
| 2. | It is associated with defining a business process and its applicability. | It helps in defining customer needs in relation to a product or service. |
| 3. | It is used for measuring the current performance of a business process. | It is used for measuring the customer needs and specifications. |
| 4. | In this, a business process is analyzed to find the root cause of a defect or recurring problem. | In this, a business process is analyzed for finding options that will help in satisfying customers. |
| 5. | In DMAIC, improvements are made in the business process for eliminating or reducing defects. | DMADV, an appropriate business model is designed that helps in meeting customer requirements. |
| 6. | In DMAIC, control systems are put in place to keep a check on future performance of a business process. | DMADV, the suggested business model is put through simulation tests for verifying efficacy in meeting customer needs and specifications. |

### 9.11.3 Benefits of Six Sigma

There are numerous benefits of six sigma as a way to address issues and problems. The most important benefit of six sigma is the reduction in defects that are allowed to reach the customer. Other benefits of six sigma include:

- Focus on customers.
- Improved customer loyalty.
- Reduced cycle time.
- Less waste.
- Data based decisions.
- Time management.
- Sustained gains and improvements.
- Systematic problem solving.
- Employee motivation
- Data analysis before decision making.
- Faster to market.
- Team building.
- Improved customer relations.
- Assure strategic planning.
- Reductions of incidents.
- Measure value according to the customer.
- Better safety performance.
- Understanding of processes.
- Effective supply chain management.
- Design and redesign products/services.
- Knowledge of competition, competitors.
- Develop leadership skills.
- Break-down barriers between departments and functions.
- Management training.
- Improve presentation skills.
- Integration of products, services and distribution.
- Use of standard operating procedures.
- Better decision making.
- Improving project management skills.
- Greater market share.
- Supervisor training.
- Lower costs to provide goods and services.
- Fewer customer complaints.

## 9.12 ENTERPRISE RESOURCE PLANNING (ERP)

When computers came in 1960s, they were mighty and costly machines and needed special skills to operate. Big companies used them for the purpose of handling business data; work like ledgering was performed on them. Enterprise resource planning software, or ERP, aims at giving an integrated software solution to all business aspects.

### 9.12.1 Meaning and Definitions of ERP

Enterprise resource planning (ERP) is defined as: 'an integrated computer based planning technique used in organizations and enterprises for management and resource planning'. Resources here mean both internal and external resources of an organization. Various resources of an organization can include financial resource, tangible resource, human resource and also various material requirements. Basically what ERP systems do is that, it integrates and automates processes within an entire organization regardless of the organization's behaviour.

A traditional definition of Enterprise Resource Planning (ERP) as given by American Production and Inventory Control Society, (APICS) – The Association for Operations Management, is given below:

**Important Point**: *"ERP is a method for effective planning and control of all resources needed to take, make, ship and account for customer orders in a manufacturing, distribution or Service Company."* -American Production and Inventory Control Society (APICS)

ERP can also be defined as:

**Important Point**: *"An ERP system is an attempt to integrate all functions across a company to a single computer system that can serve all those functions' specific needs."*

*"An application and software architecture that facilitates Information flows between various business functions inside and outside of an organization. It consolidates business environment into a uniform system environment."*

ERP are used in various industries and organizations like manufacturing, distribution, transportation, education, healthcare, banking and others. ERP delivers a single database that contains all data for the various software modules.

ERP typically addresses areas such as shown in Fig. 9.9 :

(i) **Manufacturing resource planning.** MRP involved working on complex bill of material to compute the material requirement considering production targets, stocks in hand, ordering positions, engineering, bills of materials, scheduling, capacity, workflow management, quality control, cost management, manufacturing process, manufacturing projects and manufacturing flow.

(ii) **Supply chain management (SCM).** Order to cash, inventory, order entry, purchasing, product configuration, supply chain planning, supplier scheduling, inspection of goods, claim processing and commission calculation.

(iii) **Financial management.** General ledger, cash management, accounts payable, accounts receivable, fixed assets.

(iv) **Project management.** Billing, time and expense, performance units, activity management.

(v) **Human resource management.** Human resources, payroll, training, time and attendance, roistering benefits.

The term ERP came to describe such a software solution that addressed all the business functions in an integrated way. Once the business functions were handled electronically, a need was felt to exchange relevant information to business associates – like suppliers, customers, shareholders and so on. This meant

extending information exchange beyond the boundaries of the business establishment itself.

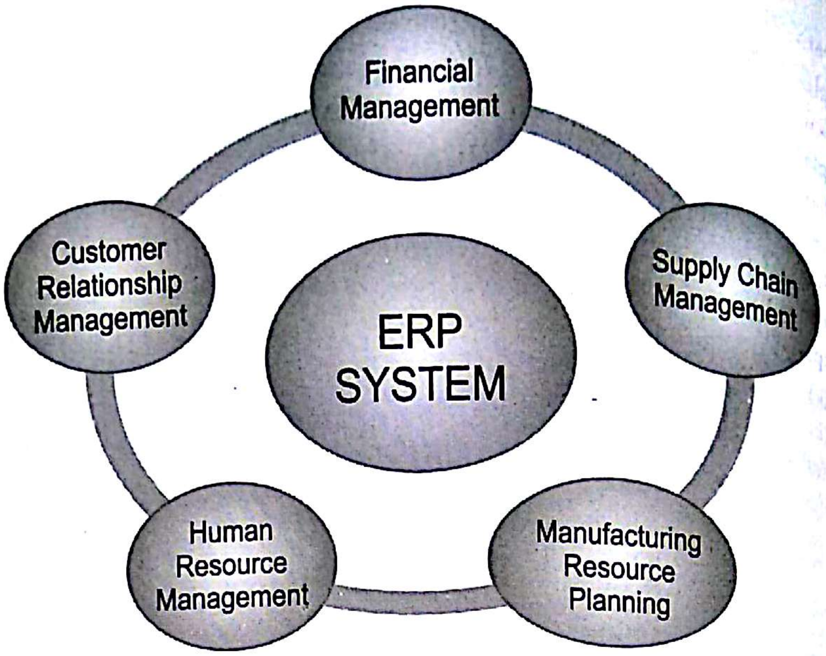


Fig. 9.9 ERP System

### 9.12.2 Major Reasons for Adopting ERP

- Integrate financial information.
- Integrate customer order information.
- Standardize and speed up operations processes.
- Reduce inventory.
- Standardize Human Resources information.
- It may also integrate key customers and suppliers as part of the enterprise's operation.
- It provides integrated database and custom- designed report systems.
- It adopts a set of "best practices" for carrying out all business processes.

**Advantages of Enterprise Resource Planning (ERP):**

- Ease of use.
- General purpose.
- Totally integrated system.
- Readymade solutions for most of the problems.
- Integration of all functions already established.
- Dependency on Human Resources eliminated.
- Suppliers and customers can do online communication.

In India, IGNOU has become the first central University in the country to integrate all its business process in back office automation by implementing Enterprise Resource Planning (ERP) successfully at its headquarters in New Delhi.

## REVIEW QUESTIONS

1. What are the various steps in method improvement?
2. Explain operations management.
3. Discuss the need to provide various allowances in determining of standard time.
4. Explain the concept of total quality management (TQM).
5. What are the different components of cost of quality?
6. Explain JIT approach?
7. What are QFD and TPM?
8. Write a short note on application of six sigma in production.
9. Explain the following:
   (a) Total productive maintenance (TPM)
   (b) Six sigma quality ($6\sigma$)
   (c) Enterprise resource planning (ERP)

# 10 Basic Concepts of Entrepreneurship

**Chapter Outline**

- Introduction
- Concepts of Entrepreneurship
- Entrepreneur
  - ⇒ Definition and Meaning
  - ⇒ Characteristics of Entrepreneur
  - ⇒ Key Qualities of Entrepreneur
  - ⇒ Types of Entrepreneur
  - ⇒ Functions of Entrepreneur
  - ⇒ Merits and Demerits of a good Entrepreneur
- Entrepreneurship
  - ⇒ Definition and Meaning
  - ⇒ Evaluation of Entrepreneurship
  - ⇒ Nature and Characteristics of Entrepreneurship
  - ⇒ Importance of Entrepreneurship
  - ⇒ Entrepreneurship and Economic Development
- Enterprise
  - ⇒ Definition and Meaning
  - ⇒ Objective of enterprise

## 10.1 INTRODUCTION

The concept of entrepreneurship has developed over the years. Many factors have contributed to the high unemployment rate while formal wage employment is decreasing very fast. Self employment is also alike entrepreneurship that is increasing and offering more job opportunities. Thus as an individual, should endeavour to learn the basic skills involved in entrepreneurship to help to set up your own business or enterprise. An exposure to entrepreneurship skills will stimulate others towards different opportunities beside wage employment. Besides, the skills one should guide your everyday work and experiences develop your entrepreneurial traits that motivate you to establish your own enterprise and subsequently create jobs for others and improve upon your own quality of life and that of your families through better job opportunities. This unit is interesting and practical. You can use the ideas and skills in your everyday life.

## 10.2 CONCEPTS OF ENTREPRENEURSHIP

In order to know what being enterprising is all about we need to understand the following terms- Entrepreneur, Entrepreneurship, and Enterprise. The concepts of entrepreneurship can explained with the help of given below Fig. 10.1.

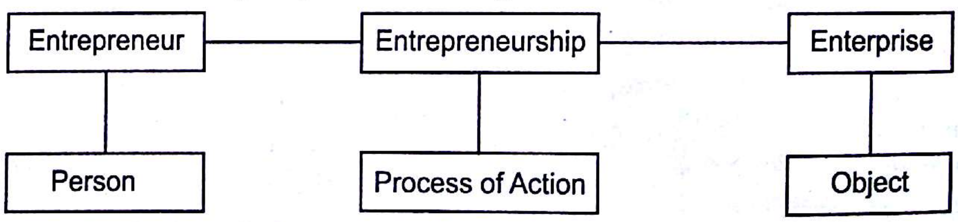


**Fig. 10.1 Concepts of Entrepreneurship**

1. **Entrepreneur:** An entrepreneur is an enterprising individual who builds capital through risk. He is the person who starts an enterprise. He searches for change and responds to it.
2. **Entrepreneurship:** It can be defined by describing what entrepreneurs do. Entrepreneurship can be described as a process of action an entrepreneur undertakes to establish his enterprise.
3. **Enterprise:** An enterprise is the business organization that is formed and which provides goods and services, creates jobs, contributes to national income, exports and over all economic development.

The brief discussions of the above terms are as following:

## 10.3 ENTREPRENEUR

[redacted]

The word 'entrepreneur' is derived from the French word '*entreprendre*' which means between takers. Entrepreneur is another name of risk owner.

### 10.3.1 Definition and Meaning

An entrepreneur is an enterprising individual who builds capital through risk. He is the person who starts an enterprise. He searches for change and responds to it. Entrepreneur in English is a term applied to a person who is willing to launch a new venture or enterprise and holds the entire responsibility for the outcome.

A number of definitions have been given of an entrepreneur:

The sociologists feel that certain communities and cultures promote entrepreneurship. The economists view him as a fourth factor of production along with land, labour and capital. Others feel that entrepreneurs are innovators who come up with new ideas for products, markets or techniques.

Some definitions of an entrepreneur are listed below:

**Important Point:** *"An entrepreneur is a person who pays a certain price for a product to resell it at an uncertain price, thereby making decisions about obtaining and using the resources while consequently admitting the risk of enterprise".* *Richard Cantillon*

- *An entrepreneur is an economic agent who unites all means of production- land of one, the labour of another and the capital of yet another and thus produces a product. By selling the product in the market he pays rent of land, wages to labour, interest on capital and what remains is his profit. He shifts economic resources out of an area of lower and into an area of higher productivity and greater yield.*
- *According to him entrepreneurs are innovators who use a process of shattering the status quo of the existing products and services, to set up new products, new services.* *Schumpeter*

*"An entrepreneur searches for change, responds to it and exploits opportunities. Innovation is a specific tool of an entrepreneur hence an effective entrepreneur converts a source into a resource".*

*"Entrepreneur is an entrepreneur within an already established organization".* *G. Pinchot*

The word 'entrepreneur' has been taken from the French language where it framed and originally meant to designate an organizer of musical or other entertainments. Oxford English Dictionary (in 1897) also defined an entrepreneur in similar way as "the director or a manager of public musical institution, one who 'gets –up' entertainment, especially musical performance". In the early

16th century, it was applied to those who were engaged in military expeditions. It was extended to cover civil engineering activities such as construction and fortification in the 17th century.

**Richard Cantillon**, an Irish man living in France, was the first who introduced the term 'entrepreneur' and his unique risk-bearing function in economics in the early 18th century. He defined entrepreneur as an agent who buys factors of production at certain prices in order to combine them into a product with a view to selling it at uncertain prices in future. Knight also described entrepreneur to be a specialized group of persons who bear uncertainty. Uncertainty is defined as a risk which cannot be insured against and is incalculable. He thus, draws a distinction between ordinary risk and uncertainty.

### 10.3.2 Characteristics of Entrepreneur

Entrepreneurs are different from each other, but successful entrepreneurs share certain common characteristics. Not all of them have developed each of the following to the same degree, but they tend to have developed most of them to some degree. Here are some common characteristics of successful entrepreneurs as shown in Fig. 10.2.

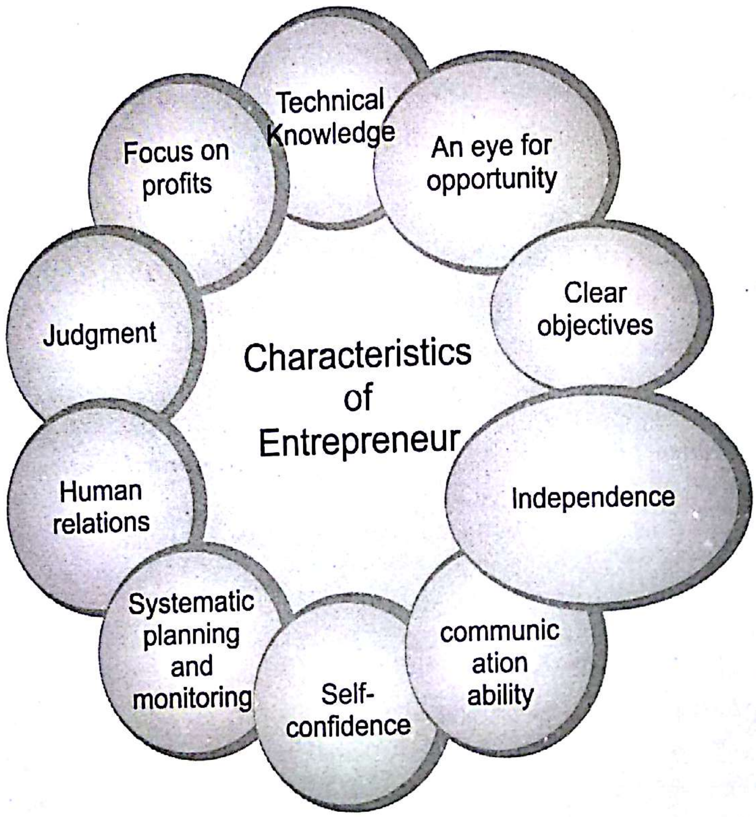


**Fig. 10.2** Characteristics of Entrepreneur

1. **An eye for opportunity:** Many entrepreneurs start by finding a need and quickly satisfying it. They do things before other asked to work by people or forced by situation.
2. **Clear objectives:** He must have clear objectives as to the exact nature of business or the nature of goods to be produced.

3. **Independence:** Even though most entrepreneurs know how to work within the framework for the sake of profits, they enjoy being their own boss.
4. **Communication ability:** He should have good communication skills which means both the sender and the receiver should understand each other's message.
5. **Self-confidence:** Entrepreneurs must demonstrate extreme self-confidence in order to cope with all the risks of operating their own business.
6. **Information seeking:** An entrepreneur undertakes personal research on how to satisfy customers and solve problems. He knows that different people have different capabilities that can be of help to them. He seeks relevant information from his/her clients, suppliers, agencies, competitors and others. He always wants to learn things which will help the business to grow up.
7. **Commitment to work:** An entrepreneur will work long hours after into the night just to be able to keep his promise to his client. He does the work together with his team to get a job done. He knows how to make people happy to work for him/her due to his dynamic leadership quality.
8. **Systematic planning and monitoring:** An entrepreneur makes plans according to his expectations in the business. He does not leave things to luck. He plans by breaking large tasks down into small once and puts time limits against them. Since an entrepreneur knows what to expect at anytime he is able to change plans and strategies to achieve what he aims at.
9. **Judgment:** Successful entrepreneurs have the ability to think quickly and make a wise and appropriate decisions.
10. **Ability to accept change:** Change occurs frequently when you own your own business, the entrepreneur thrives on changes and their businesses grow.
11. **Human Relations:** He must maintain good relation with his customers, employees, etc. To maintain good relationship he should have emotional stability, personal relations, tactfulness and consideration.
12. **Discipline:** Successful entrepreneurs resist the temptation to do what is unimportant or the easiest but have the ability to think through to what is the most essential.
13. **Technical Knowledge:** He should have sufficient technical knowledge and skills.
14. **An appetite for hard work:** Most entrepreneurs start out working long, hard hours with little pay.
15. **Focus on profits:** Successful entrepreneurs always have the profit margin in sight and know that their business success is measured by profits.

### 10.3.3 Key Qualities of an Entrepreneur

Being an entrepreneur is about more than just starting a business and the drive to succeed in business. All successful entrepreneurs have a similar way of thinking and posses several key personal qualities that make them so successful in business. All successful entrepreneurs have the following qualities as shown in Fig. 10.3:

1. **Inner drive to succeed and self- confident:** Entrepreneurs are driven to succeed and expand their business. They see the bigger picture and are often very ambitious. Entrepreneurs set massive goals for themselves and stay

committed to achieving them regardless of the obstacles that get in the way. Self confidence is a key entrepreneurial skill for success. It is easy to become demoralized, frustrated and resentful if you lack self-confidence. Self-confidence is concerned with how a person feels about his ability. A successful entrepreneur believes in his abilities.

2. **Strong Belief in themselves and must know how to rise again when he stumbles:** Failure is not the end of the game. Instead, it should be considered as a challenge and as the start of another business chapter. Through failures, one learns to cope up and recover, as experience is gained at each circumstance. Successful entrepreneurs have a healthy opinion of them and often have a strong and assertive personality. They are focused and determined to achieve their goals and believe completely in their ability to achieve them. Their self optimism can often been seen by others as ostentation or arrogance but entrepreneurs are just too focused to spend too much time thinking about unconstructive criticism.

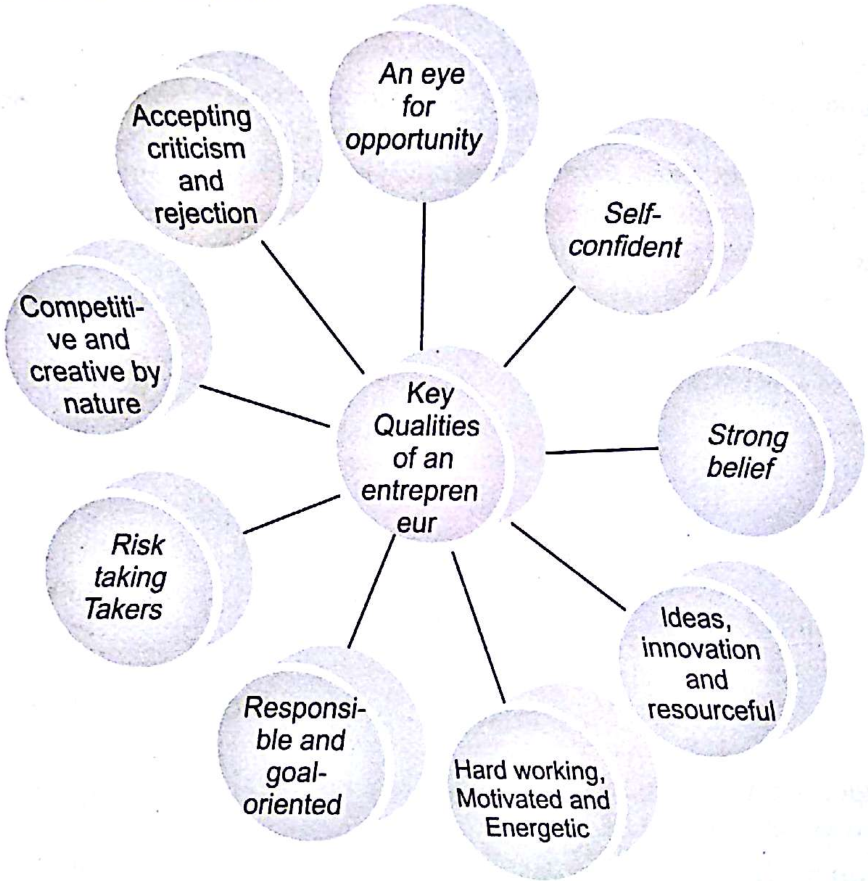


Fig.10.3 Key Qualities of Entrepreneur

3. **Search for New Ideas, Innovation and Resourceful:** All entrepreneurs have a passionate desire to do things better and to improve their products or services. They are constantly looking for ways to improve. They are creative, innovative and resourceful. Just like the foregoing attribute, they must learn how to stand up from a fall, must have enough courage to recover and face the business fray once more. In the process, as they continues, they are also ought to discover, invent and devise ways on how to correct their previous mistakes and so prevent them from recurring.

4. **Hard working, Highly motivated and energetic:** Successful entrepreneurs

are determined and hardworking. They have self-discipline to such extent that if a work is important and related to their goals, they will, eventually, complete it. Getting things done is the vital link between motivations and their outcome. Entrepreneurs are always on the move, full of energy and highly motivated. They are driven to succeed and have an abundance of self motivation. The high standards and ambition of many entrepreneurs demand that they have to be motivated!

5. **Responsible and goal-oriented:** Successful entrepreneurs try to hold entire responsibility for their actions. They know what they are today, and what they are going to be tomorrow, depend solely on themselves, as it is the outcome of their own choices and decisions. They are proactive people, who set goals, walk an extra mile to achieve them and above all rely on their own resources and abilities. Successful entrepreneurs are capable of leading people and get work done by them. They use a combination of various methods- effective motivation, planning, coaching and evaluation- to lead people. They are concerned about the wellbeing of others and easily get along with people.
6. **Risk taking:** Risk taking-successful entrepreneurs must have ability to face with any risk, evolved from the action taking. And also, they must capable to find out any new solutions in their business matters or problems.
7. **Competitive and creative by nature:** Successful entrepreneurs thrive on competition. The only way to reach their goals and live up to their self imposed high standards is to compete with other successful businesses. Creativity is the ability to use your insights and come up with new solutions to old problems, get things done in different way or find a totally different approach for conventional things to work together. Entrepreneurs need creative thinking ability virtually in everything. Each new product, each new marketing method, each business decision-all these are fertile ground for creative thinking.
8. **Accepting Criticism and Rejection:** Innovative entrepreneurs are often at the forefront of their industry so they hear the words "it cannot be done" quite a bit. They read just their path if the criticism is constructive and useful to their overall plan, otherwise they will simply disregard the comments as pessimism. Also, the best entrepreneurs know that rejection and obstacles are the part of any leading business and they deal with them appropriately.

### 10.3.4 Types of Entrepreneur

Types of entrepreneurs can be classified on different basis as shown in Fig. 10.4. The entrepreneurs who come under this basis are as follows:

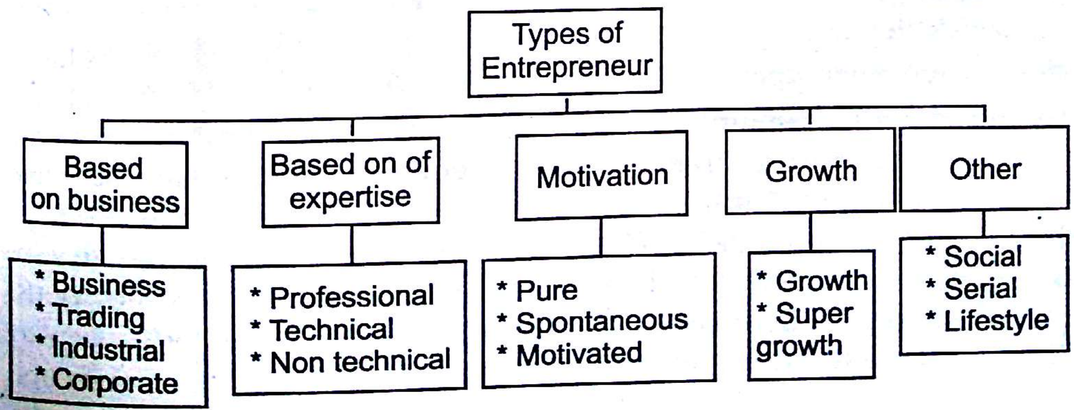


**Fig. 10.4** Types of Entrepreneur

1. **Entrepreneurs based on type of business:** The entrepreneurs on the base of business types are as following:
   - *(i)* **Business entrepreneur:** These convert ideas into reality deal with both manufacturing and trading aspect of business (LG, Samsung etc.).
   - *(ii)* **Trading entrepreneurs:** Undertake trading activities but not concerned with the manufacturing work. Identify potential markets, stimulate demand for its product line and creates a desire and interest among buyers (C&F agents, dealers).
   - *(iii)* **Industrial entrepreneur:** Undertakes manufacturing activities only new product development etc. (textile, electronics, etc).
   - *(iv)* **Corporate entrepreneur:** Interested in management part of organization exceptional organizing, coordinating skills to manage a corporate undertaking (Ambani's, Tata's, Birla's).
2. **Entrepreneurs based on expertise:** The entrepreneurs on the base of expertise types are as following:
   - *(i)* **Professional entrepreneurs:** Focus more on establishing a business but not in managing or operating it. Sell out the running business and start another venture with the sales proceeds. Conceive new ideas to develop alternative projects.
   - *(ii)* **Technical entrepreneur:** Production oriented, possesses innovative skills in manufacturing, quality control, etc.
   - *(iii)* **Non technical entrepreneur:** Develops marketing, distribution facilities and strategies.
3. **Entrepreneurs based on motivation levels:** These can be classifying as following:
   - *(i)* **Pure entrepreneurs:** Motivated by psychological and economic rewards. Undertake an entrepreneurial activity for his personal satisfaction in work, ego or status.
   - *(ii)* **Spontaneous entrepreneur:** Born entrepreneurs with inborn traits of confidence, vision and initiative.
   - *(iii)* **Motivated entrepreneurs:** Influenced by the desire for self fulfillment. They come into being because of the possibility of making and marketing of some new product for the consumer.
4. **Growth:** The entrepreneurs on the base of growth are two types:
   - *(i)* **Growth entrepreneur:** One who enters a sector with a high growth rate is a positive thinker.
   - *(ii)* **Super growth entrepreneur:** One who enters a business and shows quick step and upward growth curve.
5. **Other:** Some other types of entrepreneur are:
   - *(i)* **Social entrepreneur:** A social entrepreneur is motivated by a desire to help, improve and transform social, environmental, educational and economic conditions.
   - *(ii)* **Serial entrepreneur.** A serial entrepreneur is one who continuously comes up with new ideas and starts new businesses. In the media, the serial entrepreneur is represented as possessing a higher propensity for risk, innovation and achievement.

(iii) **Lifestyle entrepreneur:** A lifestyle entrepreneur places passion before profit when launching a business in order to combine personal interests and talent with the ability to earn a living.

### 10.3.5 Functions of Entrepreneur

An entrepreneur is a person who has control of a new enterprise, venture or idea and is accountable for the inherent risks and the outcome. Some of the major functions of an entrepreneur are as shown in Fig. 10.5:

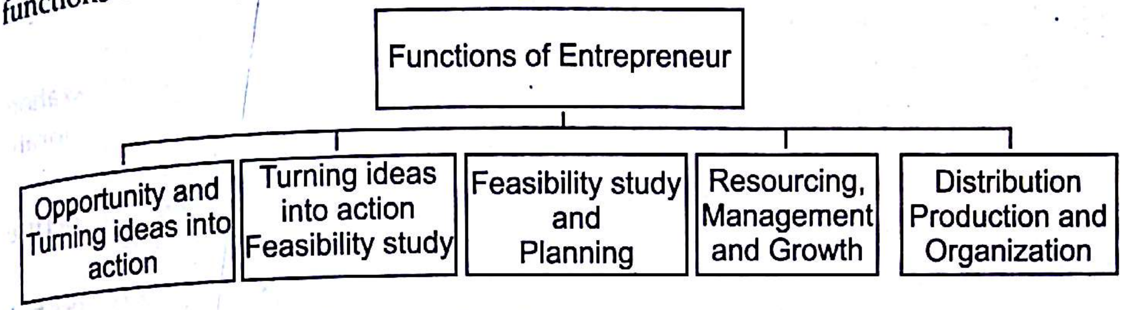


**Fig. 10.5** Functions of Entrepreneur

1. **Identifying entrepreneurial opportunity:** There are many opportunities in the world of business. These opportunities are not realized by common man, but an entrepreneur senses the opportunities faster than others do. These are based on human needs like food, style, education, etc., which are constantly changing. An entrepreneur therefore, has to keep his eyes and ears open and require imagination, creativity and informativeness.
2. **Turning ideas into action:** An entrepreneur collects information regarding the ideas, products, practices to suit the demand in the market. He should be capable of turning his ideas into reality. Further steps are taken to achieve the goals in the light of the information collected.
3. **Feasibility study:** The entrepreneur conducts studies to assess the market feasibility of the proposed product or services. He anticipates problems and assesses quantity, quality, cost and sources of inputs required to run the enterprise. Such a blue print of all the activities is termed as a 'business plan' or a 'project report'.
4. **Planning of the project:** He is the organizer to conceive the idea of launching the project and to program the structure of business.
5. **Resourcing:** The entrepreneur needs various resources in terms of money, machine, material, and men to running the enterprise successfully. An essential function of an entrepreneur is to ensure the availability of all these resources.
6. **Setting up of the Enterprise:** For setting up an enterprise the entrepreneur may need to fulfill some legal formalities. He also tries to find out a suitable location, design the premises, install machinery and do many other relevant things.
7. **Management:** The entrepreneur is also responsible for the management of business. He tries to have a least cost combination of factors of production.
8. **Face Risks:** He faces uncertainly and bears risks in his business uncertainly comprising those risks against which it is not possible to insure. He also faces the risk of other producers may enter the market.

9. **Growth and Development**: Once the enterprise achieves its desired results, the entrepreneur has to explore another higher goal for its proper growth and development. The entrepreneur is not satisfied only with achieving a set goal but constantly strives for achieving excellence.
10. **Distribution of Rewards and sale of products**: He is responsible of distributing the rewards to all factors of production. He pays the reward in the shape of rent, wage, and interest and bears the risk of profit or loss himself. An entrepreneur is also responsible of marketing and advertising. He wants to maximize his profits by selling his product in the market.
11. **Scale of Production**: He decided the scale of business in according with the provision of capital. Then, he takes the decision of what where and how to produce goods.
12. **Joint stock Organization**: In a partnership, the entrepreneurial functions are divided between the partners. But in public limited company, the board of directors takes this responsibility with nationalized enterprise; the entrepreneurial decisions are left to the government or a body to which government has delegated its powers.

### 10.3.6 ▌ Merits and Demerits of a good Entrepreneur

Entrepreneur enjoys the freedom of making their own business decisions and becoming their own bosses. In addition he also gains the stability and control that could never be achieved as a regular employee. The merits and demerits of entrepreneur are as following.

#### *10.3.6.1 Advantages of Entrepreneurs:*

1. **Excitement**: If compared with regular employees, entrepreneurs enjoy much excitement beginning from the planning stage of the business up to development and realization. Thrill-seekers obviously love being entrepreneurs as they are exposed to too much risk.
2. **Salary Potential**: Entrepreneur earns money that is equal to their efforts. On other hand most people who are employed generally feel that they are not being paid for the work they do. In addition they must follow the salary structure set by their employers.
3. **Flexibility**: Having control of work schedules and commitments makes the life of these entrepreneurs fortunate. They are able to take vacations anytime and spend much quality time with their families.
4. **Independence**: Some people wish to be their own boss and make all the important decisions himself. For people who love the idea of not being accountable to anyone else but themselves, becoming an entrepreneur would surely be wonderful. They would be able to make decisions without the pressure of getting fired.
5. **Salary potential:** Generally, people want to be paid for the amount of work they do in full and they do not want to be short-changed.
6. **Freedom:** Entrepreneurs can work whenever they want, wherever they want, and however they want.

### 10.3.6.2 *Disadvantages of Entrepreneurs:*

1. **No Regular Salary:** When you start a business, you should be prepared to leave behind the security of having a paycheck each month. Even successful entrepreneurs experience lean months when all financial resources are being taken up by the new business.
2. **Work Schedule:** Although they have the luxury of a flexible schedule, entrepreneurs also make sacrifices especially during situations that require them to work longer hours. Unlike regular employees who are not worried too much about the status of the business, entrepreneurs must make sure that everything is going well.
3. **Benefits:** There will undoubtedly be fewer benefits, especially when considering that your business will be just starting off.
4. **Administration:** Because they own the business, all major decisions are made by entrepreneurs. This is quite a burden and handling such responsibility is quite difficult. Every decision directly affects the future of their businesses and avoiding costly mistakes is imperative.

After comparing the advantages and disadvantages, you will have to decide if you can realistically handle all the responsibilities of owning your own business aside from being prepared for all the risks you have to take. But if you look closely, being an entrepreneur is still desirable especially with the sense of fulfillment and accomplishment they gain from beating all odds and overcoming all challenges. As long as you have passion and commitment, you will be able to handle these disadvantages beautifully.

## 10.4 ENTREPRENEURSHIP

Entrepreneurship can be defined by describing what entrepreneurs perform. Entrepreneurship can be described as a process of action an entrepreneur undertakes to establish his enterprise.

> **Important Point:** *"Entrepreneurs use personal initiative, and engage in calculated risk-taking, to create new business ventures by raising resources to apply innovative new ideas that solve problems, meet challenges, or satisfy the needs of a clearly defined market."*

Entrepreneurship involves bringing about change to achieve some benefit. This benefit may be financial but it also involves the satisfaction of knowing you have changed something for the better.

> **Important Point:** *"Entrepreneurship is essentially the act of creation requiring the ability to recognize an opportunity, shape a goal, and take advantage of a situation. Entrepreneurs plan, persuade, raise resources, and give birth to new ventures."*

Entrepreneurship is a creative activity. It is the ability to create and build something from practically nothing. It is an ability of sensing opportunity where others see contradiction and confusion. Entrepreneurship is the attitude of mind to seek opportunities, take calculated risks and obtain benefits by setting up a venture. It comprises of numerous activities involved in conception, creation and running an enterprise.

**Important Point:** *Entrepreneurship is defined as "a systematic innovation, which consists in the purposeful and organized search for changes, and it is the systematic analysis of the opportunities such changes might offer for economic and social innovation." Peter Drucker*

- *"Entrepreneurship is meant the function of seeking investment and production opportunity, organizing an enterprise to undertake a new production process, raising capital, hiring labour, arranging the supply of raw materials, finding site, introducing a new technique and commodities, discovering new sources of raw materials and selecting top managers of day to day operations of the enterprise." B. Higgins*

Entrepreneurship is a process. It is not a combination of some stray incidents. It is the purposeful and organized search for change, conducted after systematic analysis of opportunities in the environment. Entrepreneurship is a philosophy-it is the way one thinks, one acts and therefore it can exist in any situation be it business or government or in the field of education, science and technology or poverty alleviation or any others.

### 10.4.1 Evaluation of entrepreneurship

Entrepreneurship is an elusive concept. Emergence of entrepreneurial class is as old as our ancient history itself. History of entrepreneurship and emergence of entrepreneurial class in India may be presented in two sections as shown in the Fig. 10.6:

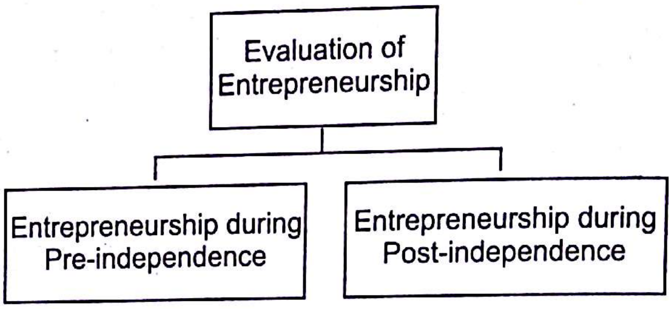


Fig. 10.6 Evaluation of entrepreneurship

1. **Entrepreneurship during pre-independence:** Before India came into contact with West Indian towns were mostly religious and aloof from the general life of country. Organized industrial activity was observable among the Indian artisans in a few recognizable products in the cities of Banaras, Allahabad & Gaya Puri. Mirzapur much prestigious Indian handicraft industry which was basically a cottage and small sector declined at the end of the $18^{th}$ century for various reasons. Some scholars hold the view that manufacturing entrepreneurship in India emerged as the latent and manifest consequence of east India company advent in India.
2. **Entrepreneurship during post-independence:** Several entrepreneurial phases in India have passed since independence. A slow pace of development was reflected in the late 1950s and early 1960s, as the entire economy was changing from an agro based economy to an industrialized economy. Soon after that the upcoming entrepreneurs got support from the government as well. A number of SSI sprouted up in late 1960s and 1970s. Here an intensive movement was initialized for further promotion of entrepreneurship. Finally, in 1980 India was able to liberalize imports and began with small and medium

scale entrepreneurs. Further, the economic reforms were introduced in 1990. It was a kind of disillusion for the budding Indian entrepreneurs and now in the 2000 the entrepreneurial scenario has undergone a vast change. Now India is taking part in global entrepreneurship as well.

## 10.4.2 Nature and Characteristics of Entrepreneurship

To understand entrepreneurship in business and industry it is important to understand the features of entrepreneurship. The most important features of entrepreneurship are explained below:

1. **Accepting Challenges:** Entrepreneur should accept the challenges created in the society due to change in situation, happening, or uncertainty.
2. **Risk Taking (Accepting):** Giving birth to a new enterprise involves risk. Doing something new and different is also risky. The enterprise may earn profit or incur loss, which depends on various factors like changing customer preferences, increased competition, shortage or raw materials, etc. An entrepreneur needs to be bold enough to assume the risk involved and hence an entrepreneur is a risk-bearer not risks avoider. This risk-bearing ability keeps him to try on and on which ultimately makes him to succeed. The Japanese proverb "Fall seven times, stand up eight" applied to entrepreneur.
3. **Innovation:** Innovation is doing something new or something different. Entrepreneurship uses inventions and adopts innovations in the organization. For example in order to satisfy the changing needs of the customers, now-a-days fruit juice (mango, apple, etc.) is being served in tins, instead of bottles so that customers can carry it and throw away the containers after drinking the juice.
4. **Manage money wisely:** The lifeblood of any business enterprise is cash flow. We need it to buy inventory, pay for services, promote and market your business, repair and replace tools and equipment, and pay yourself so that you can continue to work.
5. **Remember it is all about the customer:** The business is not about the prices that you charge for your goods and services and not about your competition and how to beat them. Your business is all about your customers, or clients, period.
6. **Project a positive business image:** The moment passing makes a positive and memorable impression on people with whom you intend to do business. The owners must go out of their way and make a conscious effort to always project the most professional business image possible.
7. **Invest in yourself:** Top entrepreneurs buy and read business and marketing books, magazines, reports, journals, newsletters, websites and industry publications, knowing that these resources will improve their understanding of business and marketing functions and skills.
8. **Sales benefits:** Pushing product features is for inexperienced or wannabe entrepreneurs. Selling the benefits associated with owning and using the products and services you carry is what sales professionals worldwide focus on to create buying excitement and to sell, sell more, and sell more frequently to their customers. Advertising, sales presentations, printed marketing

materials, product packaging, website, newsletters, trade show exhibit and signage are vital.

9. **Design workspace for success:** Carefully plan and design office workspace to ensure maximum personal performance and productivity and, if necessary, to project professionalism for visiting clients.
10. **Ability to multitask:** It's difficult for most business owners not to take a hands-on approach. They try to do as much as possible and tackle as many tasks as possible in their business. The ability to multitask, in fact, is a common trait shared by successful entrepreneurs.
11. **Follow-up constantly:** Constant contact, follow-up, and follow-through with customers, prospects, and business alliances should be the mantra of every home business owner, new or established. Constant and consistent follow-up enables you to turn prospects into customers, increase the value of each sale and buying frequency from existing customers, and build stronger business relationships with suppliers and your core business team. Follow-up is especially important with your existing customer base, as the real work begins after the sale. It's easy to sell one product or service, but it takes work to retain customers and keep them coming back.

### 10.4.3 Importance of Entrepreneurship

Entrepreneurism has been found to be a vital part of the economy. Entrepreneurship is increasingly recognized as an important driver of economic growth, productivity, innovation and employment, and it is widely accepted as a key aspect of economic dynamism: the birth and death of firms and their growth and downsizing. As firms enter and exit the market, theory suggests that the new arrivals will be more efficient than those they displace. Existing firms that are not driven out are forced to innovate and become more productive in order to compete. Entrepreneurship is important in following way:

1. **Provides employment:** Wealth and a high majority of jobs are created by small businesses started by entrepreneurially minded individuals, many of whom go on to create big businesses. Often hold a view that all those who do not get employed anywhere jump into entrepreneurship.
2. **Key driver of economy:** People exposed to entrepreneurship frequently express that they have more opportunity to exercise creative freedoms, higher self esteem, and an overall greater sense of control over their own lives. As a result, many experienced business people political leaders, economists, and educators believe that fostering a robust entrepreneurial culture will maximize individual and collective economic and social success on a local, national, and global scale.
3. **Contributed towards research and development system:** Many innovations are due to the entrepreneurs. Without the boom of inventions the world would have been a much dry place to live in. Inventions provide an easier way of getting things done through better and standardized technology.
4. **Wealth for nation and for individuals:** All individuals who search business opportunities usually create wealth by entering into entrepreneurship. The wealth created by the same play a considerable role in the development of nation. The business as well as the entrepreneur contributes in some or other way to the economy, may be in the form of products or services or boost up

the GDP rates or tax contributions. Their ideas, thoughts, and inventions are also a great help to the nation.

5. **Improvement in per capital income:** Entrepreneurs are always on the lookout for opportunities. They explore and exploit the opportunities. It will result in the increase of the overall productivity and per capita income in the country.
6. **Improvement in the standard of living:** By making efficient use of the resources, they start producing more of better quality and that too at lower costs. This enables those to ensure easy availability of better quality products at lower prices to the consumers which result in the improvement in the standard of living of the people.
7. **Provides self sufficiency:** The entrepreneur not only become self sufficient but also provide great standards of living to its employees. It provides opportunity to a number of people working in the organization.
8. **Facilitating overall development:** With the setting up of an enterprise the process of industrialization is set in motion. This unit will generate demand for various types of inputs required by it and there will be so many other units which will require the output of this unit. This leads to overall development of an area due to increase in demand and setting up of more and more units there. Entrepreneurs, thus, create an environment of enthusiasm and convey a sense of purpose. This gives future impetus to the overall development of that area.

### 10.4.4 Entrepreneurship and Economic Development

**Important Point:** "Economic development is the effect for which entrepreneurship is a cause".

Entrepreneurship helps in the process of economic development in the following ways as shown in Fig. 10.7:

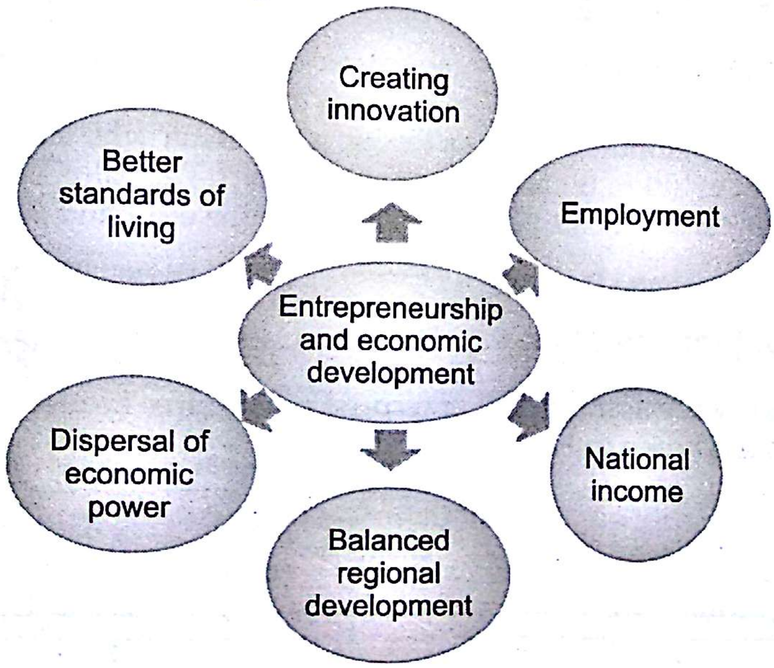


**Fig. 10.7** Entrepreneurship and Economic Development

1. **Employment:** Unemployment is the problem of any nation. Entrepreneurs generate employment both directly and indirectly. Directly, self employment

as an entrepreneur and indirectly by starting many industrial units they offer jobs to millions. So, entrepreneurship is the best way to fight the evil of unemployment.

2. **National Income:** National income consists of the commodities and services produced in the country and imported. An increasing number of entrepreneurism is required to meet this increasing demand for goods and services. Thus entrepreneurship increases the national income of any country.
3. **Balanced Regional Development:** Public benefits like transport facilities, health, education, entertainment and industries are concentrated in selected cities, development gets limited to these cities. When the new entrepreneurism grow at a faster rate, in view of increasing competition in and around cities, they are forced to set up their enterprises in the smaller towns away from big cities. This helps in the development of backward regions.
4. **Dispersal of economic power:** Developing a large number of entrepreneurism helps in dispersing the economic power amongst the population. Thus it helps in weakening the harmful effects of monopoly.
5. **Better standards of living:** Entrepreneurism helps to produce goods at lower cost and supply quality goods at lower price to the community according to their requirements. When the price of the commodities are lesser the consumers get the power to buy more goods for their satisfaction. In this way they can increase the standard of living of the people.
6. **Creating innovation:** An entrepreneur is a person who always tries to introduce newer and newer technique of production of goods and services. An entrepreneur brings economic development through innovation. In short, the development of the entrepreneurship is inevitable in the economic development of the country.

## 10.5 ENTERPRISE

An enterprise is the business organization that is formed and which provides goods and services, creates jobs, contributes to national income, exports and over all economic development. Entrepreneur is a person who starts an enterprise. The process of creation is called entrepreneurship. The entrepreneur is the actor and entrepreneurship is the act. The outcome of the actor and the act is called the enterprise.

### 10.5.1 Objectives of enterprise

We here classify the objectives of enterprise under three heads and then examine them briefly as shown in Fig. 10.8.

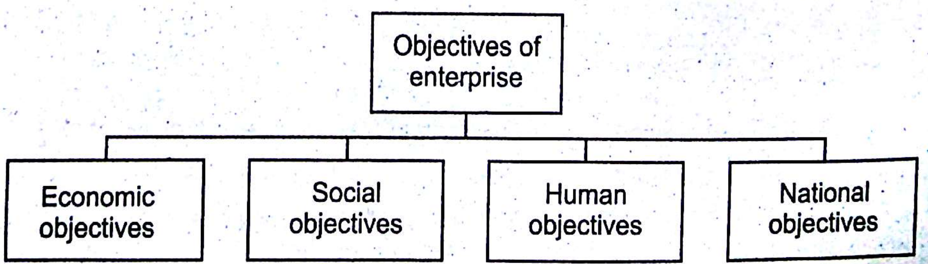


Fig. 10.8 Objectives of enterprise

1. **Economic Objectives.** Business, as we know is primarily an economic activity. The major economic objectives to be achieved by business are:
   - Profit earning
   - Creating markets
   - Technological improvements
2. **Social Objectives.** The social objectives of business are gaining more and more recognition with each passing year. The main social objectives of business are as follows:
   - Supply of standard quality of goods,
   - Avoidance of anti-social and unethical practices,
   - Provision of generating more employment,
   - Cooperation with the government,
   - Optimum utilization of national resources.
3. **Human Objectives.** The human objectives of business are that:
   - The employees working in a business should be fairly rewarded,
   - A healthy climate is created by providing opportunities to the employers,
   - The employees should have say in the affairs which directly affect them,
   - Thinking of modern business must go well beyond material benefits of its employees.
4. **National Objectives.** Every business whether operating on small or large scale must have an obligation towards nation also by achieving national goals such as promoting social justice, increasing valued added goods for exports, finding out better and cheaper substitutes for imports and helping in increasing exports for building the foreign exchange reserves to meet the import bills.

## REVIEW QUESTIONS

1. What do you mean by entrepreneur? Explain the characteristics of entrepreneur.
2. Explain the key qualities of entrepreneur.
3. Explain the different types of entrepreneur.
4. What are the main functions of entrepreneur? Explain the merits and demerits of a good entrepreneur.
5. What do you mean by entrepreneurship? Explain the evaluation of entrepreneurship.
6. Explain the nature and characteristics of entrepreneurship.
7. Explain the importance of entrepreneurship.
8. What are relationships between entrepreneurship and economic development?
9. Explain the basic concepts of entrepreneurship.
10. What is enterprise? Explain its objectives.

# 11 Theories of Entrepreneur

**Chapter Outline**

- Introduction
- Theories of Entrepreneur
- Sociological Theories
- Economic Theories
- Cultural Theories
- Psychological Theories
- Entrepreneur Traits and Behaviour
- Roles in Economic Growth
  - ⇒ Employment
  - ⇒ Social Stability
  - ⇒ Export Promotion
  - ⇒ Indigenization
- Creating a Venture
- Entrepreneur Development Program

## 11.1 INTRODUCTION

Entrepreneurship theories and research remain important to the development of the entrepreneurship field. Several theories have been proposed by scholars to explain the field of entrepreneurship. These theories offer us a fairly good opportunity to re-focus our efforts at integrating the diverse viewpoints. These theories have their roots in economics, psychology, sociology, anthropology, and management. The multi-disciplinary nature of entrepreneurship has been given a close examination in this chapter.

## 11.2 THEORIES OF ENTREPRENEUR

Entrepreneurship is an evolved thing. With the advancement of science and technology it has undergone alteration change and emerged as a critical input for socio-economic development. Various authors have developed various theories on entrepreneurship and popularized the concept among the common people. The theories propounded by them can be categorized under as shown in Fig. 11.1:

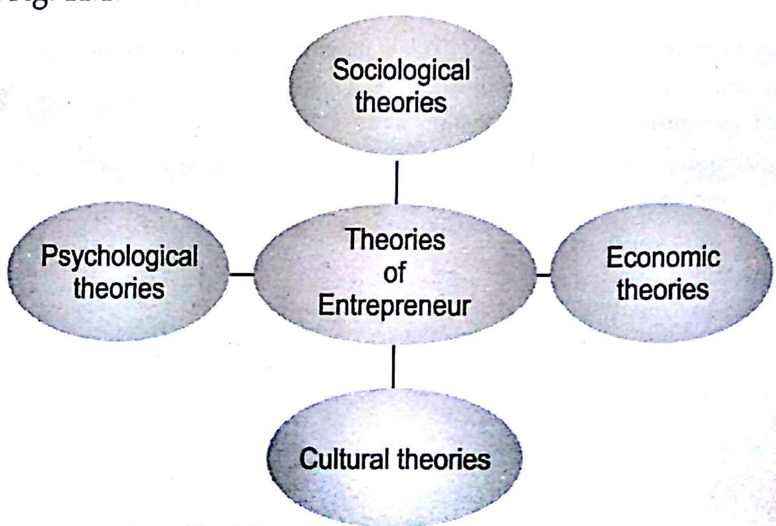


Fig. 11.1 Theories of Entrepreneur

## 11.3 SOCIOLOGICAL THEORIES

The following theories explain how sociological factors speed up the growth of entrepreneurs. According to this theory entrepreneurship is likely to get heighten in a particular social culture. Society's values, religious beliefs, customs, taboos influence the behaviour of individuals in a society. The entrepreneur is a role performer according to the role expectations by the society.

### 11.3.1 Max Weber's Theory

Max Weber (1947) analyzed religion and its impact on economic organization of the society. According to him religious beliefs are the driving or restraining force for generating entrepreneurial activity. The religious beliefs play a crucial role in determining the behaviour or actions of the entrepreneur towards generating or limiting profit. Weber is the first among the social scientists, who took the position that entrepreneurial growth is dependent upon the ethical values of society.

Salient features of Max Weber theory are:

1. Highlight Spirit of Capitalism
2. Adventurous spirit facilitate taking risk
3. Protestant ethic embodying rebellion is conducive
4. Inducement of profit is the criterion

### 11.3.2 E.E. Hagen's Theory

Theory of social change Everett E. Hagen, in his theory of social change propounded how a traditional society becomes one in which continuing technical progress takes place. The theory exhorts the following feature which presumes the entrepreneur's creativity as the key element of social transformation and economic growth. Presentation of general model of the society- the theory reveals a general model of the society which considers inter-relationship among physical environment, social structure, personality and culture, economic growth, product of social change and political change.

According to Hagen, most of the economic theories of underdevelopment are inadequate. Rejection of follower's syndrome: Hagen rejected the idea that the solution to economic development lies in imitating western technology. So, the follower's syndrome on the part of the entrepreneur is discouraged.

Salient features of his theory are:

1. Reveals general model of the social- inter-relationship among physical environment, social structure, personality and culture.
2. Thinks economic theories are inadequate.
3. Political and social change – catalyst for entrepreneurs.
4. Rejects follower's syndrome imitating western technology as the technology is an integral part of socio- cultural complex.
5. Historic shift as a factor initiates change.

## 11.4 ECONOMIC THEORIES

Entrepreneurship and economic growth take place when the economic conditions are favourable. Economic incentives are the main motivators for entrepreneurial activities. Economic incentives include taxation policy, industrial policy, sources of finance and raw material, infrastructure availability, investment and marketing opportunities, access to information about market conditions, technology, etc. Economic development takes place when a country real national income increases overall period of time wherein the role of entrepreneurs is an integral part.

### 11.4.1 Schumpeter's Theory of Innovation

Schumpeter's theory of entrepreneurship is a pioneering work of economic development. Development according to this theory implies that carrying out of new combination of entrepreneurship is basically a creative activity. According to Schumpeter an entrepreneur is one who perceives the opportunities to innovate, *i.e.*, to carry out new combinations or enterprise. In his views, the concept of new combination leading it innovation covers the following concepts:

1. The introduction of new goods and services of a new quality that is the one with which consumers are not yet familiar.
2. The introduction of new method of production.
3. The opening of new market.
4. The conquest of new source of supply of raw material.
5. The carrying out of new organization.

Salient features of Schumpeter's theory are as shown in Fig.11.2:

1. **Invention and innovation**: Schumpeter makes a distinction between innovation and invention. Invention means creation of new things and innovation means applicable of new things into practical use.
2. **Emphasis on entrepreneurial function**: In his views, development means basic transformation of the economy that is brought about by entrepreneurial functions.

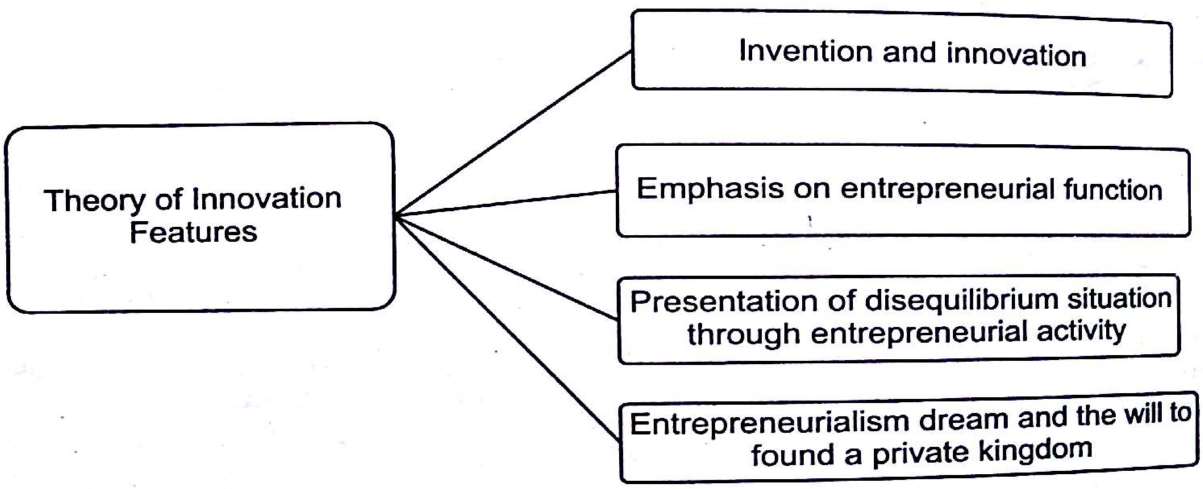


Fig. 11.2 Theory of Innovation

3. **Presentation of disequilibrium situation through entrepreneurial activity:** The entrepreneurial activity represents a disequilibrium situation, a dynamic phenomenon and a break from the routine or a circular flow or tendency towards equilibrium.
4. **Entrepreneurialism dream and the will to found a private kingdom:** The motives of creating things and applying these things into practice inspire the entrepreneur to undertake innovation.

### 11.4.2 HBS ( Harvard Business School) Theories

During the 1940s and 1950s business historians pioneered the study of entrepreneurship. The interdisciplinary Center for Research on Entrepreneurial History, based at Harvard Business School which included Joseph Schumpeter and Alfred Chandler, and its journal Explorations in Entrepreneurial History were key institutional drivers of the research agenda.

However the study of entrepreneurship ran into dreadful methodological roadblocks, and attention shifted to the corporation, leaving the study of entrepreneurship fragmented and marginal. Nevertheless business historians have made significant contributions to the study of entrepreneurship through their diverse coverage of countries, regions and industries, and – in contrast to much management research over the past two decades - through exploring how the economic, social, organizational, and institutional context matters to evaluating entrepreneurship.

HBS consider entrepreneurship is the outcome of the combination of internal and external forces as follows:

**Internal forces**- Individual's traits and qualities viz:

- Intelligence
- Skill
- Knowledge
- Intuition
- Exposure and experience

**External forces**– Surrounding's conditions viz:

- Economic
- Political
- Social and cultural
- Legal frame-work: Stable Govt. External security, law & order and legal process are the influencing factors.

## 11.5 CULTURAL THEORIES

Schumpeter remained silent about as to why some economics had more entrepreneurial talent than others. However, despite the above criticisms, Schumpeterian theory is regarded as one of the best theory in the history of entrepreneurial development.

The culture theories point out that entrepreneurship is the product of culture. Entrepreneurial talents come from cultural values and cultural system embedded into the cultural environment.

### 11.5.1 ▌ Hoselitzs Theory

Berthold Frank Hoselitz taught Economics and Social Science at the University of Chicago between 1945 and 1978. Hoselitz's Theory Hoselitz explains that the supply of entrepreneurship is governed by cultural factors, and culturally minority groups are the spark-plugs of entrepreneurial and economic development in many countries, entrepreneurs have emerged from a particular socio-economic class. He emphasized the role of culturally marginally groups like Jews and the Greeks in medieval Europe, the Chinese in South Africa and Indian in east Africa in promoting economic development. Psychological Theories Psychological theories centre's around the psychological characteristic so the individual in a society. Psychological characteristics affect the supply of entrepreneurs in the society as shown in Fig.11.3.

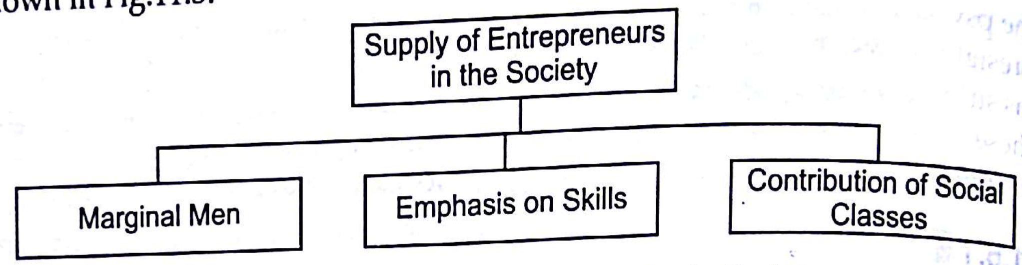


Fig. 11.3 Supply of Entrepreneurs in the Society

1. **Marginal men:** Reservoir of entrepreneurial development. Ambiguous positions from a cultural or social statement make them creative.
2. **Emphasis on skills:** Peoples who possess extra-ordinary skills like function of managerial additional personal traits and leadership skills, additional personal traits, exportation of profit and ability to lend.
3. **Contribution of social classes:** Socio-economic economic background of specific classes makes them entrepreneurs. Family patterns in France, Protestants in UK/USA & Parsees in India.

### 11.5.2 ▌ Peter F. Drucker

According to Drucker, successful entrepreneurship involves the following things- Value and Satisfaction obtained from resource by the consumer are increased. New values are created, material is converted into a resource or exiting resources are combined in a new or more productive configuration.

**Important Point:** *"An entrepreneur is one who always searches for change, rapidness to it and exploits it as an opportunity."* *Peter F. Drucker*

Drucker emphasizes on:

Innovation and Resource: A thing is regarded as resource when its economic value is recognized. Example- Fixed salary can also be an opportunity. Thus installment purchase was introduced.

According to him, innovation is the real hub of entrepreneurship which creates resource. A thing is regarded as resource when its economic value is recognized. For example, mineral oil was considered worthless until the discovery of its use. Similarly, purchasing power was considered an important resource by an American innovative entrepreneur who invented installment buying.

Entrepreneurship is the practice which has a knowledge base. Entrepreneurship is not confined to big businesses and economic institutions; it is equally important to small business and non-economic institutions. Entrepreneurship behaviour rather than personality trait is more important to enhance entrepreneurship. The foundation of entrepreneurship lies in concept and theory rather than in intuition.

Thus, Drucker has given his views that "an entrepreneur need not be a capitalist or an owner. A banker who mobilizes other's money and allocates it in areas of higher yield is very much an entrepreneur though he is not the owner of the money.

## 11.6 PSYCHOLOGICAL THEORIES

The psychological characteristics include need for high achievement, a vision or foresight, ability to face opposition. Entrepreneurship gets a boost when society has sufficient supply of individuals with necessary psychological characteristics. These characteristics are formed during the individual's upbringing which stress on standards of excellence, self reliance and low father dominance.

### 11.6.1 David McClelland (1971)

He has explained entrepreneurial development from psychological perspective. According to McClelland, entrepreneurial growth can be explained in terms of need for 'achievement motivation' which he considers as the major determinant of entrepreneurial development. For McClelland 'achievement motivation' is a motivation of the people to achieve. It is a strong desire on the part of the people, if not by all but at least by some to achieve. This motivation instilled in the culture in terms of values, norms, and beliefs (what McClelland calls value attitudes). That is the reason why some cultures motivate their people towards a strong desire to achieve and while others are not.

## 11.7 ENTREPRENEUR TRAITS AND BEHAVIOR

Successful business people have many traits in common with one another. They

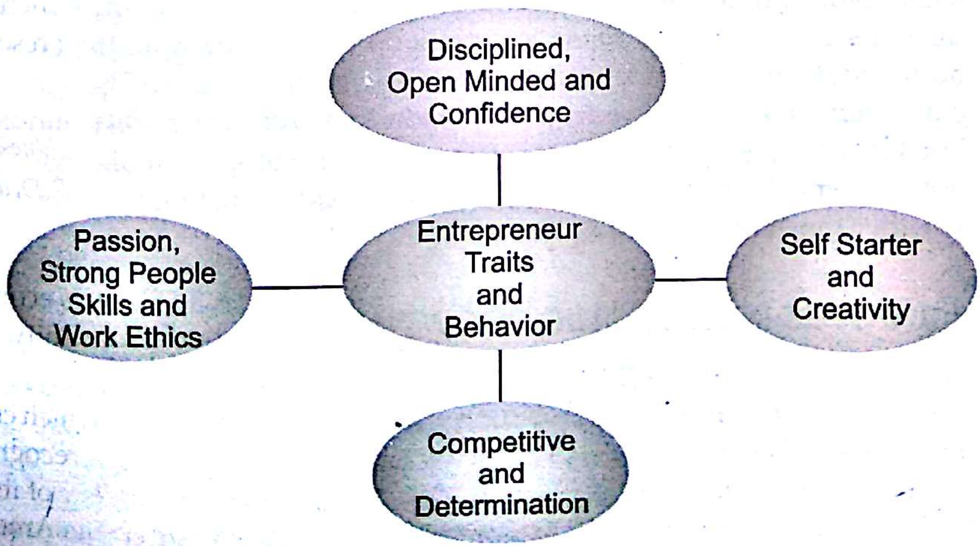


**Fig. 11.4** Entrepreneur Traits and Behavior

are open to any new ideas which cross their path. Here are some traits and behaviour of the successful entrepreneur as shown in Fig. 11.4.

1. **Disciplined, Open Minded and Confidence:** Successful entrepreneurs are disciplined enough to take steps every day toward the achievement of their objectives. Entrepreneurs realize that every event and situation is a business opportunity. Ideas are constantly being generated about workflows and efficiency, people skills and potential new businesses. They have the ability to look at everything around them and focus it toward their goals. The entrepreneur does not ask questions about whether they can succeed or whether they are valuable of success. They are confident with the knowledge that they will make their businesses succeed.
2. **Self Starter and Creativity:** Entrepreneurs know that if something needs to be done, they should start it themselves. They set the parameters and make sure that projects follow that path. They are practical and not waiting for someone to give them permission. One facet of creativity is being able to make connections between seemingly unrelated events or situations. Entrepreneurs often come up with solutions which are the synthesis of other items. They will repurpose products to market them to new industries.
3. **Competitive and Determination:** Many companies are formed because an entrepreneur knows that they can do a job better than another. They need to win at the sports they play and need to win at the businesses that they create and run. An entrepreneur will highlight their own company's track record of success. Entrepreneurs are not saddened by their defeats. They look at defeat as an opportunity for success. They are determined to make all of their endeavors succeed, so they try and try again until the task is accomplished. Successful entrepreneurs do not believe that something cannot be done.
4. **Passion:** Passion is the most important trait of the successful entrepreneur. They genuinely love their work. They are willing to put in those extra hours to make the business succeed because the happiness their business gives which goes beyond the money. The successful entrepreneur will always be reading and researching ways to make the business better and better.
5. **Strong people skills and work ethic:** The entrepreneur has strong communication skills to sell the product and motivate employees. Most successful entrepreneurs know how to motivate their employees so the business grows overall. They are very good at highlighting the benefits of any situation and educating others to their success. The successful entrepreneur will often be the first person to arrive at the office and the last one to leave. They come to their office during holidays to make sure that an outcome meets their expectations. Their mind is constantly on their work, whether they are in or out of the workplace.

## 11.8 ROLES IN ECONOMIC GROWTH

The entrepreneurs' scans, analyze and identify opportunities in the environment transform them into business proposition through creation of economic growth with their ability.

**Important Point:** *"Development does not occur spontaneously as a natural consequence when economic conditions in some sense are right."*

*Meir and Baldwin*

*"The rate of economic progress of a nation depends upon its rate of innovation which is turn depends on rate of increase in the entrepreneurial talent in the population." Joseph Schumpeter*

Entrepreneurs plays important role in economics growth of any country as shown in Fig. 11.5.

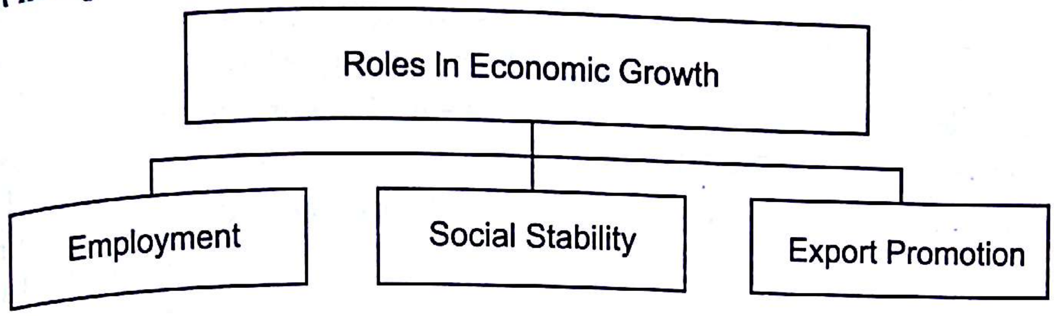


**Fig. 11.5** Roles in Economic Growth

### 11.8.1 Employment

This is the real attraction of being an entrepreneur. They are not the job seekers but job creators and job providers. With the globalization process the government jobs are shrinking leaving many unemployed. In this circumstances, the entrepreneurs and their enterprises are the only hope and source of direct and indirect employment generation. Employment is generated directly by the requirement of the large enterprises and indirectly by consequential development activities.

### 11.8.2 Social Stability

Entrepreneurial initiative through employment generation leads to increase in income and purchasing power which is spent on consumption expenditure. Increased demand for goods and services enhance industrial activity. Large scale production results in economies of scale and low cost of production. Modern concept of marketing involves creating a demand and then fullfilling it. New innovative and varying quality products at most competitive prices making common man's life smoother, easier and comfortable are the contribution of entrepreneurial initiative. The social objectives of business are gaining more and more recognition. The main social objectives of business are as follows:

- Supply of standard quality of goods.
- Avoidance of anti-social practices.
- Provision of generating more employment.
- Co-operation with the government.
- Optimum utilization of available national resources.

### 11.8.3 Export Promotion

An enterprise is the business organization that is formed and which provides goods and services, creates employment, contributes to national income, exports and over all economic development. Every business whether operating on smaller

or larger scale must have an obligation towards nation also by achieving national goals such as promoting social justice, increasing valued added goods for exports, finding out better and cheaper substitutes for imports and helping in increasing exports for building the foreign exchange reserves to meet the import bills.

## 11.9 CREATING A VENTURE

Entrepreneurs have important roles in creating new businesses that stimulates progress in societies worldwide. The entrepreneur uses innovation and technology to cultivate positive impact and activity in all facets of life. The capable entrepreneur learns to identify, select, describe, and communicate the essence of an opportunity that has attractive potential to become a successful venture.

The entrepreneur is able to describe the valuable contributions of a venture and create the design of a business model that can be sustained by a competitive advantage. The venture team creates a road map (strategy) that can, with good chance, effectively lead to the commercialization of the new products or services in the marketplace with a sustainable competitive advantage.

## 11.10 ENTREPRENEUR DEVELOPMENT PROGRAM

Entrepreneurial development is a process in which person's motivational drives of achievement and insight to undertake uncertain and risky situations especially in business undertakings. The process of entrepreneurial development focuses on training, education, re-orientation and creation of conducive and healthy environment for the growth of enterprises.

**Important Point:** *EDP is an effective human resource development tool. It designed to help a person in strengthening and fulfilling his entrepreneurial motive and in acquiring skills and capabilities necessary for playing his entrepreneurial role effectively.*

### 11.10.1 Objectives of the Program

The entrepreneurial develop program have following objectives:

1. To promote the development of small and medium enterprises that would encourage self employment among potential entrepreneurs.
2. To provide, in the rural areas, special programs designed to stimulate new ventures and encourage expansion of existing activities of small and medium industries.
3. To generate employment and self employment opportunities in the processing of indigenous (home-grown) raw materials for local consumption and export.
4. To develop entrepreneurial opportunities for potential entrepreneurs and upgrade managerial skills for existing entrepreneurs.

For a sound training programme for entrepreneurship development in India, the expert group constituted by the NIESBUD accepted that it must be able to help selected entrepreneurs to:

1. Develop and strengthen their entrepreneurial quality/motivation.
2. Analyze environment related to small industry and small business.
3. Select project/product.

4. Formulate project...
5. Understand the process and procedure of setting up of a small enterprise.
6. Know and influence the source of help/support needed for launching an enterprise.
7. Acquire the basic management skills.
8. Know the pros and cons of being an entrepreneur.
9. Acquaint and appreciate the needed social responsibility/entrepreneurial disciplines.

**Some of the other important objectives of entrepreneurial programs are:**

1. To let the entrepreneur set or reset the objectives of his business and work individually and along with his group for their realization.
2. To prepare him for accepting totally unforeseen risks of business after such training.
3. To enable him to take strategic decisions.
4. To enable him to build an integrated team to fulfill the demands of future.
5. To communicate fast, clearly and effectively.
6. To develop a broad vision to see the business as a whole and to integrate is function with it.
7. To enable him to relate his product and industry to the total environment, to find what is significant in it and to take it into account in his decisions and actions.
8. To enable him to cope with and co-ordinate all relevant paper work, most of which is statutorily obligatory.
9. To make him accept industrial democracy that is accepting workers as partners in enterprise.
10. To strengthen his integrity, honesty and compliance with law.

## Review Questions

1. What are the various theories of entrepreneurship?
2. Discuss economic theories of entrepreneurship.
3. Write a note on entrepreneur traits and behaviour.
4. What are the various roles of entrepreneur in economic growth?
5. Discuss about the different sources of funds in entrepreneurship.
6. Write a short note on entrepreneur development program.

# 12. Sources of Funds

## Chapter Outline



## 12.1 INTRODUCTION

Governments and various industrial promotion and support institutions are making considerable efforts to facilitate the process of emergence of new entrepreneurs for setting up enterprises in small scale sector. These efforts involved making attractive schemes for availability of finance and various other assistances including technical know-how, training, sales, purchases, etc. It is believed that these efforts have made a favorable impact on the growth of these enterprises in the state as well as in the region. Today, there are large number of organizations and financial institutions like Industrial Development Bank of India (IDBI), Small Industries Development Bank of India (SIDBI) and various commercial banks in particular. This chapter will examine the role of financial institutions in promoting small scale and tiny industries in terms of growth of entrepreneurs, enterprises and its contribution to State Domestic Products involved in entrepreneurship development activities in the region.

## 12.2 COMMERCIAL BANK

Banks have developed around 200 years ago. The nature of banks have changed as the time has changed. The term bank is related to financial transactions. Commercial banks help to mobilize savings of the people for productive purposes. They collect scattered and idle savings of people, pool them together and make fund available for productive purposes.

- Meaning of Regulation and Control of Industries
- Need and Objectives Regulation of Industries
- Different Types of Regulatory Authorities

**Important Point:** *"A bank is an institution whose debts are widely accepted in settlement of other people's debts to each other."*
*Prof. Sayers*

In this definition Sayers has emphasized the transactions from debts which are raised by a financial institution.

**Important Point:** *"A banking company means any company which transacts the business of banking. Banking means accepting for the purpose of lending of investment of deposits of money from the public, payable on demand or other wise and withdraw able by cheque, draft or otherwise."*
*Indian Banking Company Act 1949,*

### 12.2.1 Objectives of commercial banks

The main objective of a commercial bank is to generate profitability for its ownership by providing quality based products and services to the residents of the communities and regions that they represent. Some of other objectives are as following:

1. **Encourages savings:** With the existence of commercial banks and with attractive incentives such as high interest rates, etc. the people are encouraged to save more.
2. **Encourages investments:** Commercial banks provide short-term and medium-term loans for industries, trade and commerce at reasonable rates of interest. Easy loans attract the investors to invest in new enterprises.
3. **Development of agricultural sector:** The process of loans to agriculture sector has greatly helped in increasing agricultural production and income of the farmers. Commercial banks provide easy loans to farmers for the purpose of buying tractors, threshers, installation of tube-wells, purchase of fertilizers, seeds, etc.
4. **Promotes foreign trade:** Commercial banks promote foreign trade, by financing the foreign trade of a country by granting loans, opening letter of credit, discounting foreign bills of exchange and issuing bank drafts.
5. **Finances Government Projects:** Commercial banks help the government when it faces financial crisis. In order to provide funds or public projects, banks purchase government securities. This is a type of loan to the government for the purposes of development projects, etc.
6. **Development of Industrial Sector:** Commercial banks provide short-term and medium-term loans to industry. Commercial banks not only provide finance for the development of industry but also help the industry in many other ways. Commercial banks play an important role in expansion and development of industrial sector in a country.
7. **Capital Formation:** The commercial banks play an important role in all the three stages of capital formation. Capital formation means an increase in the stock of capital goods in the economy such as increase in number of production units, plant, machinery etc.
8. **Implementation of monetary policy:** The central bank of the country (in India- Reserve Bank of India) forms the monetary policy to control and regulate volume of credit in the country.

## 12.2.2 Functions of commercial banks

The main function of commercial banks is to accept deposits from the public and advancing them loans. It satisfies the financial needs of the sectors such as agriculture, industry, trade, communication, etc. However, besides these functions there are many other functions which these banks perform. Generally the functions of commercial banks are divided into two categories viz. primary functions and the secondary functions as shown in Fig. 12.1.

Functions of Commercial Banks

| Primary Functions | Secondary Funtions |
|---|---|
| 1. Accepting Deposits | 1. Clearance of Cheque |
| 2. Making Advances | 2. Sale/Purchase of Shares/Bonds |
| 3. Credit Creation | 3. Transfer of Money |
| | 4. To work as Trustee |
| | 5. To work as a representative |
| | 6. To give/accept money |
| | 7. To provide letter of credit |

**Fig. 12.1** Functions of Commercial Bank

1. **Primary functions of commercial banks:** Commercial banks performs various primary functions some of them are given below:
   (i) **Accepting Deposits:** The most important function of commercial banks is to accept deposits from the public. Various sections of society, according to their needs and economic condition, deposit their savings with the banks. For example, fixed and low income group people deposit their savings in small amounts for the point of view of security, income and saving promotion. On the other hand, traders and businessmen deposit their savings in the banks for the convenience of payment.
   (ii) **Making Advance loans:** The second important function of commercial banks is to advance loans to its customers. Banks charge interest from the borrowers and this is the main source of their income. Banks advance loans not only on the basis of the deposits of the public rather they also advance loans on the basis of depositing the money in the accounts of borrowers. In other words, they create loans out of deposits and deposits out of loans. This is called as credit creation by commercial banks.
   Modern banks give mostly secured loans for productive purposes. In other words, at the time of advancing loans, they demand proper security or collateral. Generally, the value of security or collateral is equal to the amount of loan. This is done mainly with a view to recover the loan money by selling the security in the event of non-refund of the loan.
   (iii) **Credit creation:** It is most significant function of the commercial banks. While sanctioning a loan to a customer, a bank does not provide cash to the borrower; instead it opens a deposit account from where the borrower can withdraw. In other words, while sanctioning a loan a bank

automatically creates deposits. This is known as a credit creation from commercial bank.

2. **Secondary functions of commercial banks:** Along with the primary functions each commercial bank has to perform several secondary functions too. It includes many agency functions or general utility functions. The secondary functions of commercial banks can be divided into agency functions and utility functions.

   **(i) Agency Functions:** Various agency functions of commercial banks are:

   *(a)* Banks collect cheques, drafts, bills of exchange and dividends of the shares for their customers.

   *(b)* Banks make payment for their clients and at times accept the bills of exchange of their customers for which payment is made at the fixed time.

   *(c)* Banks pay insurance premium of their customers. Besides this, they also deposit loan installments, income-tax, interest, etc. as per directions.

   *(d)* Banks purchase and sale securities, shares and debentures on behalf of their customers.

   *(e)* Banks arrange to send money from one place to another for the convenience of their customers.

   **(ii) General utility functions:** The general utility functions of the commercial banks are:

   *(a)* To provide safety locker facility to customers.

   *(b)* To provide money transfer facility.

   *(c)* To issue traveler's cheque.

   *(d)* To act as referees.

   *(e)* To accept various bills for payment e.g., phone bills, gas bills, electricity bills, water bills, etc.

   *(f)* To provide merchant banking facility.

   *(g)* To provide various cards such as credit cards, debit cards, smart cards, etc.

   *(h)* During natural calamities, banks are highly useful in mobilizing funds and donations.

## 12.3 FINANCING INSTITUTIONS

A financial institution is an institution that provides financial services for its clients or members. Probably the most important financial service provided by financial institutions is acting as financial Peace Corps. Most financial institutions are regulated by the government.

Financial institutions include banks, credit unions, asset management firms, building societies, and stock brokerages, among others. These institutions are responsible for distributing financial resources in a planned way to the potential users. There are a number of institutions that collect and provide funds for the necessary sector or individual. On the other hand, there are several institutions that act as the middleman and join the deficit and surplus units.

### 12.3.1 ▌Types of Finance Institutions

Financial institutions can be categorized as follows:

1. **Depositary Institutions:** Deposit-taking are those institutions that accept and manage deposits and make loans, including banks, building, societies, credit unions, trust companies, and mortgage companies.
2. **Contractual Institutions:** The insurance companies and pension funds comes in this category. These companies operate in a number of countries. On the other hand, there are insurance companies that provide coverage for a variety of risk factors and they also provide several investment options. Insurance companies provide loans for a number of purposes and create investment products.
3. **Investment Institutes:** The functions of financial institutions like investment banks are also vital and related to the investment sector. These companies are involved in a number of financial activities, such as underwriting securities, selling securities to investors, providing brokerage services, and fund raising advice.

### 12.3.2 ▌Functions of Finance Institutions

Financial institutions provide service as intermediaries of financial markets. They are responsible for transferring funds from investors to companies in need of those funds. Financial institutions facilitate the flow of money through the economy. To do so, savings are brought to provide funds for loans. Some of Finance Institution is as follow:

***1. RESERVE BANK OF INDIA (RBI)***

The Reserve Bank of India was established on April 1, 1935 in accordance with the provisions of the Reserve Bank of India Act, 1934. The Central Office of the Reserve Bank was initially established in Calcutta but was permanently moved to Mumbai in 1937. **Sir Osborne Arkell Smith**, was the first Governor of the Reserve Bank of India from April 1, 1935 to June 30, 1937.

Though originally privately owned, since nationalization in 1949, the Reserve Bank is fully owned by the Government of India. **Sir Chintaman Dwarakanath Deshmukh** was an **Indian civil servant and the first Indian** to be appointed as the Governor of the Reserve Bank of India in 1943 by the British Raj Authorities. The Central Office is where the Governor sits and where policies are formulated.

The Reserve Bank of India performs this function under the guidance of the Board for Financial Supervision (BFS). The Board was constituted in November 1994 as a committee of the Central Board of Directors of the Reserve Bank of India.

***OBJECTIVES OF RBI***

Primary objective of BFS is to undertake consolidated supervision of the financial sector comprising commercial banks, financial institutions and non-banking finance companies.

The board is constituted by co-opting four Directors from the Central Board as members for a term of two years and is chaired by the Governor. The Deputy Governors of the Reserve Bank are ex-officio members. One Deputy Governor,

usually, the Deputy Governor in charge of banking regulation and supervision, is nominated as the Vice-Chairman of the Board.

The board is required to meet normally once every month. It considers inspection reports and other supervisory issues placed before it by the supervisory departments.

BFS through the Audit Sub-Committee also aims at upgrading the quality of the statutory audit and internal audit functions in banks and financial institutions. The audit sub-committee includes Deputy Governor as the chairperson and two Directors of the Central Board as members.

The BFS oversees the functioning of Department of Banking Supervision (DBS), Department of Non-Banking Supervision (DNBS) and Financial Institutions Division (FID) and gives directions on the regulatory and supervisory issues.

***MAIN FUNCTIONS OF RBI***

The Preamble of the Reserve Bank of India describes the basic functions of the Reserve Bank as:

> **Important Point:** *"...To regulate the issue of Bank Notes and keeping of reserves with a view to securing monetary stability in India and generally to operate the currency and credit system of the country to its advantage."*

**Some of the other functions of RBI are as follows:**

- Formulates implements and monitors the monetary policy.
- Regulator and supervisor of the financial system.
- Regulator and supervisor of the payment systems.
- Authorizes setting up of payment systems.
- Lays down standards for operation of the payment system.
- Issues direction, calls for returns/information from payment system operators.
- Manages the Foreign Exchange Management Act, 1999 (FEMA).
- Issues and exchanges or destroys currency and coins not fit for circulation.
- Performs a wide range of promotional functions to support national objectives.
- Banker to the government: performs merchant banking function for the central and the state governments; also acts as their banker.
- Banker to banks: maintains banking accounts of all scheduled banks.

***2. INDUSTRIAL FINANCE CORPORATION OF INDIA (IFCI)***

As stated earlier, the Industrial Finance Corporation of India was the first All India Development Bank to be set up in the country. It was set up in 1948 with the object of providing medium and long-term credit to industry. As pointed out earlier, its role was that of gap filler as it was not expected to compete with the prevailing channels of industrial finance. It was only meant to supplement their efforts. In the beginning, the IFCI was expected to extend financial assistance only to industrial concerns in the private and cooperative sectors. Now both public sector and joint sector projects are also eligible for financial assistance from the

IFCI. With effect from July 1, 1993, IFCI has been converted into a public limited company and is now known as Industrial Finance Corporation of India Ltd.

***OBJECTIVES***

The main objective of Industrial Finance Corporation of India Limited is to provide financial assistance to large-scale industrial units particularly at a time when the normal banking accommodation is inadequate and not forthcoming to assist these industrial units. Industrial enterprises, organized on the basis of proprietary or private limited company basis, cannot take loans from this corporation. Only the public limited companies are eligible to take loans from it.

***FUNCTIONS OF IFCI***

The Industrial Finance Corporation of India grants financial assistance in the following forms:

1. Provides loans or advances both in rupees and foreign currencies repayable within 25 years.
2. Guaranteeing rupee loans floated in the open market by industrial concerns.
3. Underwriting of shares and debentures of the industrial concerns.
4. To underwrite the issue of stocks, shares, debentures or bonds to industrial units but must dispose of such securities within 7 years.
5. For setting up a new industrial undertaking.
6. For expansion and diversification of existing industrial undertaking.
7. To accept public deposits up to Rs. 10 crores for a period of five years only.
8. To act as an agent for the Central Government and for the World Bank in respect of loans sanctioned by them to industrial units.
9. To guarantee deferred payments by importers of capital goods, who all are able to obtain this concession from foreign manufacturers.
11. To provide technical guidance to industrial units as to finance (loans).
12. To guarantee loans in foreign currency.
13. To examine utility of loans granted to industrial units,
14. To guarantee loans raised from scheduled banks and State Co-operative Banks.

***3. STATE FINANCIAL CORPORATION (SFC)***

In order to meet the financial requirements of small scale and medium-sized industries, there was a need of special financial institutions. With this view, the Central Government passed the State Financial Corporation Act of September 28, 1951 which empowered the state government to establish financial corporation to operate within the state. So far (till now) 18 state financial corporations have been established in different states.

State Financial Corporations have played an important role in the development of small and medium enterprises in their respective states with the main objectives of financing and promoting these enterprises for achieving balanced regional growth, catalyze investment, generate employment and widen the ownership base of industry. With the liberalization drive getting accelerated, SFC's future business

is likely to face SFCs provides a range of financial services that utilizes sound and dynamic investment decisions to select clients aiming to protect and develop their global wealth.

### OBJECTIVE OF SFC

The State Financial Corporations (SFCs) are state-level financial institutions, operating as regional development banks playing a crucial role in the development of small and medium enterprises in the states concerned in tander with national priorities. It is based on following objectives:

1. SFC establishes uniformity in regional industries.
2. It provides incentive to new industries.
3. To bring efficiency in regional industrial units.
4. To develop regional financial resources.
5. It provides finance to small-scale, medium sized and cottage industries in the state.

### FUNCTION OF SFC

SFCs provide financial assistance by way of term loans, direct subscription to equity, debentures, guarantees, discounting of bills of exchange and seed/special capital. It has following functions:

1. It provides loans for a period not exceeding 20 years to industrial units.
2. It underwrites the issue of shares, debentures and bonds for a period not exceeding 20 years of industrial units.
3. To give guarantee to loans taken by industrial units for a period not exceeding 20 years.
4. SFC makes payment of capital goods purchased in India by these industrial units.
5. It subscribe to the share capital of the industrial units, in case they wish to raise additional capital.
6. State Financial Corporation of every state is governed by a board of directors consisting of 18 Directors in all, duly elected and nominated.
7. The State Financial Corporation can have share capital ranging from Rs. 50 lakhs to Rs. 5 crores. It can be increased up to Rs. 10 crores with the prior sanction of the Central Government.
8. The State Financial Corporation can issue bonds and debentures to a maximum of ten times the amount of its paid-up capital and reserve fund.
9. The State Financial Corporation can accept public deposits for a maximum period of 5 years. However, the total amount received by way public deposits should not exceed twice its paid-up capital.
10. Borrowings from the state government and the Reserve Bank.

### 4. INDUSTRIAL CREDIT AND INVESTMENT CORPORATION OF INDIA (ICICI)

The Industrial Credit and Investment Corporation of India (ICICI) were registered as a private limited company in 1955. It was set up as a private sector development bank to assist and promote private industrial concerns in the country.

**Broad objectives of the ICICI are:**

ICICI Bank's Green initiative is to make healthy environment in the organization *i.e.*, to create intra-personal skills amongst the customer and understanding between employees of the organization. The broad objectives of the ICICI are:

(a) To assist in the creation, expansion and modernization of private concerns;

(b) To encourage the participation of internal and external capital in the private concerns;

(c) To encourage private ownership of industrial investment.

**Functions of the ICICI**

(i) It provides long-term and medium-term loans in rupees and foreign currencies.

(ii) It underwrites new issues of shares and debentures.

(iii) It guarantees loans raised by private concerns from other sources.

(iv) It provides technical, managerial and administrative assistance to industrial concerns.

**Features of ICICI**

The important features of the functioning of the ICICI are as given below:

(i) The financial assistance as provided by the ICICI includes rupee loans, foreign currency loans, guarantees, underwriting of shares and debentures, and direct subscription to shares and debentures.

(ii) Originally, the ICICI was established to provide financial assistance to industrial concerns in the private sector. But, recently, its scope has been widened by including industrial concerns in the public, joint and cooperative sectors.

(iii) ICICI has been providing special attention to financing riskier and non-traditional industries, such as chemicals, petrochemicals, heavy engineering and metal products. These four categories of industries have accounted for more than half of the total assistance.

(iv) Of late, the ICICI has also been providing assistance to the small scale industries and the projects in backward areas.

(v) Along with other financial institutions, the ICICI has actively participated in conducting surveys to examine industrial potential in various states.

(vi) In 1977, the ICICI promoted the Housing Development Finance Corporation Ltd. to grant term loans for the construction and purchase of residential houses.

(vii) Since 1983, the ICICI has been providing leasing assistance for computerization, modernization and replacement schemes; for energy conservation; for export orientation; for pollution controller balancing and expansion: etc.

(viii) The ICICI has not contributed much to reduce regional disparities. About three-fifth of the total assistance given by the ICICI has been received by the advanced states of Maharashtra, Gujrat and Tamil Nadu.

(ix) With effect from April 1st, 1996, Shipping Credit and Investment Company of India Ltd., (SCICI) was merged with ICICI.

(x) The ICICI Ltd. was merged with ICICI Bank Ltd. effective from May 3rd, 2002.

## 5. LIFE INSURANCE CORPORATION OF INDIA (LIC)

The Life Insurance Corporation of India came into existence on July 1, 1956 and the corporation began to function on September 1, 1956. The corporation gets a large amount as insurance premium and has been investing in almost all sectors of the economy, viz., public sector, private corporate sector, co-operative sector, joint sector and now it is one of the biggest term lending institutions in the country.

Life Insurance Corporation of India (LIC) is the largest insurance group and investment company in India. It is a state-owned where Government of India has 100% stake. LIC also funds close to 24.6% of the Indian Government's expenses. Over its existence of around 50 years, Life Insurance Corporation of India, which commanded a monopoly of soliciting and selling life insurance in India, created huge surpluses, and contributed around 7% of India's GDP in 2006.

LIC Golden Jubilee Foundation was established in 2006 as a charity organization. This entity has the aim of promoting education, alleviation of poverty, and providing better living conditions for the under privileged. Out of all the activities conducted by the organization, Golden Jubilee Scholarship awards are the best known. Each year, this award is given to the meritorious students in standard XII of school education or equivalent, who wish to continue their studies and have a parental income less than Rs. 60,000/-.

### OBJECTIVE OF LIC

LIC explore and enhance the quality of life of people through financial security by providing products and services of aspired attributes with competitive returns, and by rendering resources for economic development. It has following objectives:

1. Spread life insurance widely and in particular to the rural areas and to the socially and economically backward classes with a view to reaching all insurable persons in the country and providing them adequate financial cover against death at a reasonable cost.
2. Maximize mobilization of people's savings by making insurance-linked savings adequately attractive.
3. Bear in mind, in the investment of funds, the primary obligation is to its policyholders, whose money it holds in trust, without losing sight of the interest of the community as a whole; the funds to be deployed to the best advantage of the investors as well as the community as a whole, keeping in view national priorities and obligations of attractive return.
4. Conduct business with allmost economy and with the full realization that the moneys belong to the policyholders.
5. Act as trustees of the insured public in their individual and collective capacities.
6. Meet the various life insurance needs of the community that would arise in the changing social and economic environment.
7. Involve all people working in the corporation to the best of their capability in furthering the interests of the insured public by providing efficient service with courtesy.

8. Promote amongst all agents and employees of the corporation a sense of participation, pride and job satisfaction through discharge of their duties with dedication towards achievement of corporate objective.

## FUNCTION OF LIC

The functions of the LIC shall be to carry on and develop life insurance business to the best advantage of the society.

1. To carry on capital redemption business, annuity certain business or re-insurance business in so far as such re-insurance business relating to life insurance business.
2. To invest the funds of the corporation in such manner as the corporation may think fit and to take all such steps as may be necessary or expedient for the protection or realization of any investment.
3. To transfer the whole or any part of the life insurance business carried on outside India to any other person or persons, if in the interest of the corporation it is expedient so to do.
4. To advance or lend money upon the security of any movable or immovable property or otherwise.
5. To borrow or raise any money in such manner and upon such security as the corporation may think fit.
6. To carry on either by itself or through any subsidiary any other business in any case where such other business was being carried on by a subsidiary of an insurer whose controlled business has been transferred to and vested in the corporation by this act.
7. To do all such things as may be incidental or conducive to the proper exercise of any of the powers of the corporation.
8. In discharging of any of its functions the corporation shall act so far as may be on business principles.

### *6. UNIT TRUST OF INDIA (UTI)*

The Unit Trust of India (UTI) was established on February 1, 1964 under the Unit Trust of India Act, 1963 by the government of India. Its establishment has been a landmark in the history of investment trusts in India. It completed 35 years on June 30, 1999. The UTI started the sale of units to the public from the July, 1964.

## OBJECTIVE OF UTI

The basic objective of the UTI is to offer both small and large investors the means of acquiring shares in the widening prosperity resulting from the steady, industrial growth of the country. There are two main objectives of UTI:

1. **Promote and pool the small savings:** It promotes and pools the small savings from the lower and middle income people who cannot have direct access to the stock exchange.
2. **Share the benefits and fruits:** UTI give them an opportunity to share the benefits and fruits of prosperity resulting from rapid industrialization in India.

## FUNCTIONS OF UTI

The main functions of UTI are as follows:

1. It encourages savings of lower and middle-class people.

2. To sale units to investors in different parts of the country.
3. It converts the small savings into industrial finance.
4. To give them an opportunity to share the benefits and fruits of industrialization in the country.
5. It provides liquidity to units.

## 7. INDUSTRIAL DEVELOPMENT BANK OF INDIA (IDBI)

The Industrial Development Bank of India (IDBI) was established on July 1, 1964 under an Act of Parliament as a wholly owned subsidiary of the Reserve Bank of India. The main aim behind the setting up of IDBI was to provide credit and other facilities for the Indian industry, which was still in the initial stages of growth and development. It is the 10th largest development bank in the world with 1,300 ATMs, 758 branches and 513 centers. Some of the institutions built by IDBI are:

- National Stock Exchange of India
- National Securities Depository Services Ltd
- Stock Holding Corporation of India
- Export Import Bank of India
- Small Industries Development Bank of India etc...

The year 2005 witnessed the merger of IDBI Bank with the Industrial Development Bank of India Ltd. The new entity continued to its development finance role, while providing an array of wholesale and retail banking products (and does so till date). The following year, IDBI Bank acquired United Western Bank (which, at that time, had 230 branches spread over 47 districts, in 9 states). In the financial year of 2008, IDBI Bank had a net income of Rs. 9415.9 crores and total assets of Rs. 120,601 crores.

### OBJECTIVES OF IDBI

The main objectives of IDBI are to serve as the apex institution for term finance for industry in India. Its objective includes:

1. Co-ordination, regulation and supervision of the working of other financial institutions such as Industrial Finance Corporation of India (IFCI), Industrial Credit and Investment Corporation of India Bank (ICICI), Unit Trust of India (UTI), Life Insurance Corporation of India (LIC), Commercial Banks and State Financial Corporation (SFCs).
2. To establish and carry on business of banking in all forms within India and outside India.
3. To finance, promote or develop industry and assist in the development of Industries.
4. Supplementing the resources of other financial institutions and there by widening the scope of their assistance.
5. Devising and enforcing a system of industrial growth that conforms to national priorities.
6. Planning, promotion and development of key industries and diversifications of industrial growth.
7. Promotion of employment-oriented industries, especially in semi- urban areas to create more employment opportunities and thereby checking migration of population to urban areas.

## FUNCTION OF IDBI

The major functions of IDBI are given below:

1. It re-finances loans and advances provided by the existing lending institutions to the small-scale units.
2. To grant loans and advances to scheduled banks or state co-operative banks by way of re-financing of loans granted by such institutions which are repayable in 15 years.
3. To grant loans and advances to IFCI, SFCs, other institutions, scheduled banks, state co-operative banks by way of refinancing of loans granted by such institution to industrial concerns for exports.
4. Provide fixed deposit services.
5. Provide the facilities to underwrite or to subscribe to shares or debentures of industrial concerns.
6. To subscribe to or purchase stock, shares, bonds and debentures of other financial institutions.
7. Provide the facilities to discount or re-discount bills of industrial concerns.
8. To grant line of credit or loans and advances to other financial institutions such as IFCI, SFCs, etc.
9. Personal banking likes to make payments to vendors in different cities without any costs. Receive payments from customers without any charge deducted from the amount. Do all the banking right from wherever a person travels. Most importantly, maintain better relations with the vendors and customers.
10. Provide grant loans to any industrial concern.
11. To guarantee deferred (delayed) payment due from any industrial concern.
12. To guarantee loans raised by industrial concerns in the market or from institutions.
13. To provide consultancy and merchant banking services in or outside India.

### *8. EXPORT-IMPORT BANK OF INDIA (EXIM BANK)*

Export-Import Bank of India is the premier export finance institution of the country, established in 1982 under the Export-Import Bank of India Act 1981. EXIM Bank plays four-pronged role with regard to India's foreign trade:

(i) Those of a Coordinator,
(ii) A source of Finance,
(iii) Consultant and
(iv) Promoter.

EXIM Bank is the coordinator of the Working Group Mechanism for clearance of Project and Services Exports and Deferred Payment Exports (for amounts above a certain value currently US$ 100 million). The Working Group comprises EXIM Bank, Government of India representatives (Ministries of Finance, Commerce, External Affairs), Reserve Bank of India, Export Credit Guarantee Corporation of India Limited (ECGC) and commercial banks who are authorized foreign exchange dealers.

## OBJECTIVES OF EXIM

**Important Point:** *"...for providing financial assistance to exporters and importers, and for functioning as the principal financial institution for coordinating the working of institutions engaged in financing export and import of goods and services with a view to promoting the country's international trade..."*

*"...shall act on business principles with due regard to public interest".*

## EXPORT-IMPORT BANK OF INDIA

The main functions of the EXIM Bank are as follows:

1. Financing of exports and imports of goods and services, not only of India but also of the third world countries.
2. Financing of exports and imports of machinery and equipment on lease basis.
3. Financing of joint ventures in foreign countries.
4. It providing loans to Indian parties to enable them to contribute to the share capital of joint ventures in foreign countries.
5. It undertakes limited merchant banking functions such as underwriting of stocks, shares, bonds or debentures of Indian companies engaged in export or import.
6. EXIM provides technical, administrative and financial assistance to parties in connection with export and import.

### *9. SMALL INDUSTRIES DEVELOPMENT BANK (SIDBI)*

Small Industries Development Bank of India was established as wholly owned subsidiary of Industrial Development Bank of India (IDBI) under the small Industries Development of India Act 1989. It took over the IDBI business relating to small scale industries including National Equity Scheme and Small Industries Development Fund. The objective of establishment of SIDBI, in particular, is to strengthen and broad-base the existing institutional arrangement to meet the requirement of small scale industries and tiny industries.

## OBJECTIVES OF SIDBI

In the setting up of SIDBI, the main objective of the government was to ensure larger flow of assistance to the small-scale units. To meet with this, the immediate thrust of the SIDBI was on the following measures:

1. In the initiating steps for technological up gradation and modernization of existing units.
2. For the promotion of employment-oriented industries, especially in semi-urban areas to create more employment opportunities and thereby checking migration of population to urban areas.
3. Expanding the channels for marketing the products of the small scale sector.

## FUNCTIONS OF SIDBI

SIDBI provides support to the small-scale industries sector in the country through the existing banking and other financial institutions such as SFC, State Industrial Development Corporation (SIDC), commercial banks, co-operative banks and Regional Rural Banks (RRBs), etc. The major functions of SIDBI are as follows:

1. SIDBI re-finances loans and advances provided by the existing lending institutions to the small-scale units.
2. To extends seed capital/soft loan assistance under National Equity Fund, Mahila Udyam Nidhi and Mahila Vikas Nidhi and seed capital schemes.
3. Provide discounts and re-discounts bills arising from sale of machinery and manufactured by small-scale industrial units.
4. To grants direct assistance and refinance loans extended by primary lending institutions for financing exports of products manufactured by small-scale units.
5. It provides services like factoring, leasing, etc. to small units.
6. It extends financial support to State Small Industries Corporations for providing scarce raw materials to and marketing the products of the small-scale units.
7. SIDBI provides financial support to National Small Industries Corporation for providing; leasing, hire purchase and marketing help to the small-scale units.

## 12.4 MEANING OF REGULATION AND CONTROL OF INDUSTRIES

When a market is not competitive, there is a need for regulators. Their role is to balance the interests of various stakeholders. Business organizations can use a monopoly position to create extremely high added value for the benefit of their shareholders, employees, etc. Customers need to be protected by limiting these monopoly powers. At the same time, it is necessary for the businesses to price their products at a sufficient margin.

Regulatory bodies are established in countries according to the policy of the government with different types of authorities. Regulatory rules are designed to meet government objectives. These rules should be understood by the regulator and the regulated industry.

Growth of the industrial sector at a higher rate and on a continued basis is a major determinant of a country's overall economic development. In this regard, the government of the country has issued industrial policies, from time to time, to facilitate and promote the growth of industry and maintain its productivity and competitiveness in the world market.

In order to provide the central government with the means to implement its industrial policies, several legislations have been enacted and amended in response to the changing environment. In India the most important is being the Industries Development and Regulation Act, 1951 (IDRA) which was enacted in pursuance of the Industrial Policy Resolution, 1948. The act was formulated for the purpose of development and regulation of industries in India by the Central Government.

## 12.5 NEED AND OBJECTIVES OF REGULATION OF INDUSTRIES

The main need and objectives of the regulation of Industries may be classified as follows:

- To take necessary steps for the development of industries;
- To regulate the pattern and direction of industrial development;

- To control the activities, performance and results of industrial undertakings in the public interest;
- To maintain a sustained growth in productivity;
- To achieve optimal utilization of human resources;
- To enhance gainful employment;
- To attain international competitiveness and
- To transform India into a major partner and player in the global field.

However, small scale industrial undertakings and ancillary units are exempted from the provisions of this Act.

## 12.6 DIFFERENT TYPES OF REGULATORY AUTHORITIES

Certain social objectives such as availability and affordability of services to particular groups like disabled or people in rural areas cannot be achieved from macro-economic objectives of the government. Therefore regulatory bodies are established to control and monitor these areas. Different types of regulatory authorities are as following:

1. Bank regulation
2. Consumer protection
3. Cyber-security regulation
4. Financial regulation
5. Food safety and food security
6. Occupational safety and health
7. Public health
8. Pollution
9. Telecommunication
10. Vehicles
11. Science
12. Wage regulation

## REVIEW QUESTIONS

1. What is the meaning of regulation and control of industries? Explain the need and objectives regulation of industries.
2. Explain the different types of regulatory authorities in India.
3. What is commercial banks? Explain the objectives and functions of commercial banks in India.
4. What is financing institutions? Explain the types of finance institutes.
5. What is Industrial development bank of India (IDBI). Explain the objectives and function of IDBI.
6. What do you mean by Industrial Finance Corporation of India (IFCI). Explain the objectives and functions of IFCI.
7. What is Reserve Bank of India (RBI). Explain the objectives and functions of RBI.
8. What is Life Insurance Corporation of India (LIC)? Explain the objective and function of LIC.
9. Write a short note on Unit trust of India (UTI). Explain the objectives of UIT and functions of UIT.
10. What is state financial corporation (SFC). Explain the objectives and functions of SFC.
11. What is Small Industries Development Bank (SIDBI). Explain the objectives and functions of SIDBI.
12. What is EXIM Bank? Explain the objectives and functions of EXIM Bank.

## Chapter Outline

- Introduction
- Meaning and Definition
- Need and Significance of Project Report
- Contents
- Formulation
- Network Analysis
- Errors of Project Report
- Project Appraisal
- Market Feasibility Study
- Technical Feasibility Study
- Financial Feasibility Study
- Social Feasibility Study

## 13.1 INTRODUCTION

The project report is an extremely important aspect of the project. It should be properly structured and also necessary and appropriate information regarding the project. No data fields are to be exposed in the project field.

The aim of the project is to produce a good product that you developed during the project are merely a means to this end. Design document has to be progressively converted to a project report as and when the various stages of project are completed. Ideally you should produce the bulk of the report as you go along and use the last week or two to bring it together into a coherent document.

## 13.2 MEANING AND DEFINITION OF PROJECT REPORT

A project report serves like a road map or strategy to reach the destination determined by the entrepreneur. In simple words project report or business plan is a written statement of what an entrepreneur proposes to take up. Project report is a kind of course of action what the entrepreneur hopes to achieve in his business and how he is going to achieve it.

> **Important Point:** *"A project as a scheme, design, a proposal of something intended or devised."*
>
> *-Webster New 20th century dictionary*

In other words, project report or business plan is a written statement of what an entrepreneur proposes to take up. It is a kind of guide or course of action what the entrepreneur hopes to achieve in his business and how is he going to achieve it.

## 13.3 NEED AND SIGNIFICANCE OF REPORT

An objective without a plan is a dream. A project report helps to understand the opportunities, problems and weakness of the business. The preparation of project report is of great significance for an entrepreneur. It guides the entrepreneur in actually starting up and running the business venture. It helps him to monitor

whether the business is growing as was projected in the business plan or not. The project report serves the two essential functions:

1. **Project report works like a road map/strategy:** Dan Steinhoff and John F. Burgess hold the view that without well spelled out goals and operational methods, most businesses flounder on the rocks of hard times.

   The project report is like a road map it describes the direction the enterprise is going in, what its goals are, where it wants to be, and how it is going to get there. In addition it enables the entrepreneur to know that he is proceeding in the right direction. It helps in documenting the cost estimates of the business. It can be used as a handy tool to persuade investors and financial institution to fund the project.

   It can help in proper utilization of all the available resources. It can keeps up the morale of employees, owners and investors. It can finally lead to a sustainable development of the organization.

2. **Attract lenders and investors:** It attracts lenders and investors. The preparation of project report is beneficial for the small scale enterprises. On the basis of project report, entrepreneur may apply for financial assistance from the financial institutions and commercial banks.

## 13.4 ESSENTIAL OF A PROJECT REPORT

The project report should be prepared with great care and consideration. The essential elements of project report have as following:

1. The project report should be sequentially arranged.
2. The project report should be covering all the details about the proposed project.
3. The project report should not be very lengthy and subjective.
4. The projections should be appropriately be made from 2 to 10 years.
5. The project report should justify the financial needs and financial projection.
6. The project report should also justify market prospects and demands.
7. The project report should be attractive to the financial agencies and investors.
8. The project report should be appealing and also have a high aesthetic value.

## 13.5 CONTENTS

A good project report should contain the following contents.

1. **Cover sheet and table of contents**: Cover sheet is like the cover pages of the book. It mentions the name of the project and address of the promoters. The table of contents is like the table of content of a book. It guides the person reviewing the project report to the desired section quickly. A good methodology would be, to divide the project report into section and number or label the section like 1, 2, 3… or a, b, c….
2. **General information, location, land and building:** A good project report should contain information on product profile and product details. Report should furnish the details about exact location of the project, lease or freehold, location advantages, land area, construction area, type of construction, cost of construction, detailed plan and estimate along with plant layout which will give details about the business concept. It must discuss the objective of

the business, a brief history about the past performance of the company and the form of ownership. It also label's the address of the proposed headquarters.

3. **Product, services, process and utilities:** A brief description of product/services is to be given in this sub-section. A report should contain description of production process, process chart, technical know- how, available technology alternatives and production program. It includes the key features of product and the product range that would be offered to potential customers. It also gives details. about the patents, trademarks, copyrights, franchises and licensing agreements. The report also includes the sources of utilities like the water, power, steam, compressed air requirements, and cost estimates.
4. **Man power and raw material:** Man power requirement by skilled and semi-skilled, sources of manpower supply, cost of procurement, requirement for training and its cost. The list of raw material required by quality and quantity, sources of procurement, cost of raw material, tie-up arrangements, if any for procurement of raw material, alternative raw material, if any.
5. **Marketing Plan and market:** Marketing mix strategies are to be drawn based on the market research. The market research provides information regarding the taste, needs, and habits of the customer. Market research is the backbone of success and failure of any product in the market. Based on the information collected through market research marketing mix strategies for product/ services, prices, promotion and place (distribution) are prepared.

   The budget for the marketing plan is drawn at the end. End-users of product, distribution of market (as local, national, international), trade practices, sales promotion activities, are the basis of proposed market research.
6. **Requirement of working capital and funds:** Working capital required, sources of working capital need for collateral security, nature and extent of credit facilities offered and available. This also includes break-up project cost in terms of costs of land, building machinery, miscellaneous assets, preliminary expenses, contingencies and margin money for working capital, arrangements for meeting the cost of setting up of the project.
7. **Others:** Project report contains some other information like cost of production and profitability of first ten years. Break-even analysis and schedule of implementation should also be included.

## 13.6 FORMULATION

Project formulation is an investigating process, which precedes investment decisions. It present the relevant facts before the decision enable them to accept or reject the project. So, the project idea is examined from the view point of overall objectives, financial viability, technical feasibility and social impact. The project formulation divides the process of project development into eight different and sequential stages as given below:

1. General information
2. Project description
3. Market potential
4. Capital costs and sources of finance
5. Assessment of working capital requirements

6. Other financial aspects
7. Economical and social variables
8. Project implementation

1. **General Information:** The information of general nature given in the project report includes: details of promoter their name and address, qualifications, experience and other capabilities of the entrepreneur. Industry profile are which the project belongs to, for *e.g.*, past performance, present status, its organization, its problems, etc. The constitution and organization structure of the enterprise; in case of partnership firm its registration with registrar of firms, certification from the directorate of industry/district industry centre. Product details like product utility, product range, product design, advantage to be offered by the product over its substitutes if any.
2. **Project Description:** A brief description of the project covering the following aspects should be made in the project report.
   (i) **Location of enterprise and physical infrastructure:** It includes description of owned or leasehold land, industrial area, no objection certificate (NOC) from the municipal authorities if the enterprise location falls within the residential area.
   (ii) **Raw material and skilled labour:** Requirement of raw material, whether inland or imported, sources of raw material supply, availability of skilled labour in the area, arrangements for training labourers in various skills.
   (iii) **Utilities:** These include: Requirement for power, load sanctioned, availability of power, and requirement for fuel items such as coal, oil or gas, state of their availability. The sources and quality of water should be clearly stated in the project report. Pollution control like scope of dumps; sewage system and sewage treatment plant should be clearly stated in case of industries producing emissions.
   (iv) **Communication and transport facilities:** Availability of communication facilities, *e.g.*, telephone, telex, etc. should be stated in the project report. Requirements for transport, mode of transport, potential means of transport, distances to be covered, restricted access etc., should be stated in the business plan.
   (v) **Other common facilities:** The common facilities are like machine shops, welding shops and electrical repair shops etc., should be stated in the report.
3. **Market Potential:** While preparing a project report, the following aspects relating to market potential of the product of the product should be stated in the report. It includes:
   - Demand and supply position
   - Expected price and marketing strategy
   - After sales service
4. **Capital costs and sources of finance:** An estimate of the various components of capital items like land and buildings, plant and machinery, installation costs, preliminary expenses, margin for working capital should be given in the project report. The sources should indicate the owner's funds together with funds raised from financial institutions, banks or any other sources.

5. **Assessment of working capital:** The requirement for working capital and its sources of supply should clearly be mentioned. It is preferred to prepare working capital requirements in the prescribed formats designed by limits of requirement.
6. **Other financial Aspects:** In addition to this, the break even analysis should also be presented. Break even point (BEP) is the level of production at which the enterprise shall earn neither profit nor incur loss. Breakdown level indicates the gestation period and the likely moratorium required for repayment of the loans.
7. **Economical and Social Variables:** The following socio-economic variables benefits should also be stated in the report.
   (i) Employment generation
   (ii) Import substitution and exports
   (iii) Local resource utilization and development of the area.
8. **Project Implementation:** Every entrepreneur should draw an implementation scheme or a time-table for his project to the timely completion of all activities involved in setting up an enterprise. If there is a delay in implementation, the project cost over-run. A simplified implementation schedule for a small project includes:
   1. Formulation of project report
   2. Application of term loans
   3. Term-loan sanction
   4. Possession of land
   5. Construction of building
   6. Getting power and water
   7. Placing order of machinery
   8. Receipt and installation of machinery
   9. Manpower requirement
   10. Trial production
   11. Commencement of commercial production.

## 13.7 ERRORS OF PROJECT REPORT

Entrepreneurs do make mistakes while selecting and formulating project report. Some of the common errors found in project formulation are:

1. **Selection of project area:** Entrepreneurs select wrong area of product means selection of a product without detailed study of product market, demand patterns, competition in the industry, change of customer tastes and perceptions or mistaken overview of the demand pattern. For example a marketing man in textile is likely to choose textile as his product.
2. **Market study and analysis:** The market research, study and analysis are the critical aspect for an entrepreneur in selection of a product and market segment.
3. **Selection of technology:** Wrong selection of technology leads to problems of costs, profit margins and feasibility issues of the entire project. An appropriate technology is necessary for any new enterprise for its survival and growth.

4. **Optimistic estimates:** Any business plan made by an entrepreneur based on wrong data, financial jugglery will give problems in selection and implementation of the project.
5. **Ownership form:** A suitable ownership form is to be evolved for the project to avoid stoppages, freeze and disputes.
6. **Selection of location:** Location is almost permanent to any project and as such plays an important role in cost competitiveness and viability of the organization throughout its life.

## 13.8 PROJECT APPRAISAL

Appraisal of term loan proposals (projects) is an important exercise for the financial institutions and investing companies in credit decisions. The art of project appraisal puts more emphasis on the economic and technical soundness of the project and earning potential than on the adequacy and liquidity of the security offered. Hence, the process of appraisal should require more dynamic approach as it is linked with a sense of uncertainty or risk.

Project appraisal is made for both proposed and executed projects. In case of former project appraisal is called **'ex-ante analysis'** and in case of letter **'post-ante analysis'**. Here, project appraisal is related to a proposed project. An entrepreneur needs to appraise various alternative projects before allocating the scarce resources for the best project.

Project appraisal means the assessment of a project. Project appraisal is a cost and benefits analysis of different aspects of proposed project with an objective to adjudge its viability. A project involves employment of scarce resources. Thus, project appraisal helps in selecting the best project among available alternative projects. For appraising projects its economic, financial, technical market, managerial and social aspect is analyzed. Financial institutions carry out project appraisal to assess its creditworthiness before extending finance to a project.

### 13.8.1 Method of Project Appraisal

Appraisal of a proposed project includes the following analyses as shown in Fig. 13.1:

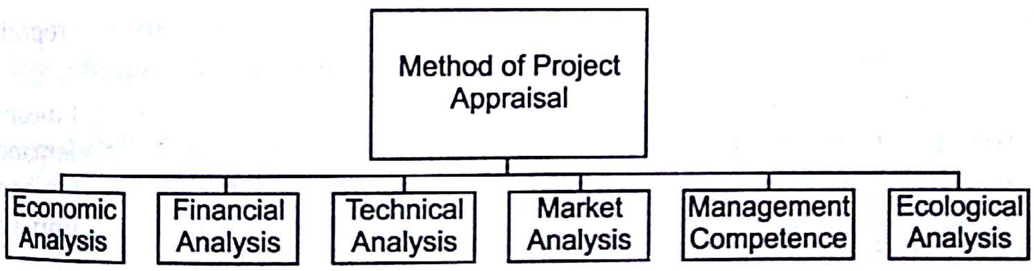


**Fig. 13.1** Method of Project Appraisal

1. **Economic Analysis:** This is one of the main methods of project appraisal. It is said that a business should have always a volume of profit clearly in view which will govern other economic variable like sales, purchase, expenses and alike. Under economic analysis the aspects highlighted includes:
   - Requirements for raw material

- Anticipated sales
- Anticipated expenses
- Level of capacity utilization
- Proposed profits
- Estimated demand

2. **Financial Analysis**: Finance is most important to establish an enterprise. It is finance only that facilitates an entrepreneur to bring together the labour, machines and raw materials to combine them to produce goods. In order to adjudge the financial viability of the project, the following aspects need to be carefully analyzed:
   - Cost of capital
   - Sources of finance
   - Estimates of sales and production
   - Cost of production
   - Working capital requirement and its financing
   - Break-even point
   - Projected cash flow
   - Projected balance sheet.

   However the enterprise sometimes fails to achieve the targeted level of capacity due to various business complications like unforeseen shortage of raw material, unexpected disruption in power supply, instability to penetrate the market mechanism, etc.

3. **Market Analysis**: Before the production actually starts, the entrepreneur needs to anticipate the possible market for the product. He has to anticipate who will be the potential customer for his product and where his product will be sold. This is because production has no value for the producer unless it is sold. In fact, the potential of the market constitutes the determinant of possible reward from entrepreneurial career. Thus knowing the anticipated market is for the product to be produced becomes an important element in any business plan. The commonly used methods to estimate the demand for a product are as follows:

   (i) **Opinion polling method**: In this method, the opinion of the ultimate users is collected. This may be attempted with the help of either a complete survey of all customers or by selecting a few consuming units out of the relevant population.

   (ii) **Life Cycle Segmentation Analysis**: It is well established that like a man, every product has its own life span as shown in Fig. 13.2.

**Important Point**: *"Life-cycle of market offering-stages of market acceptance through which a market offering passes in market offering's life-cycle are Market introduction, Market growth, Market saturation, Market decline and Market death."* *-Lipson and Darling*

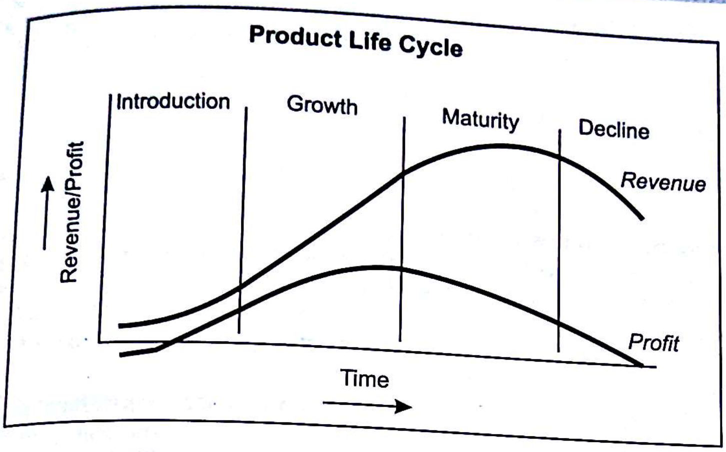


Fig. 13.2 Product Life Cycle

The characteristics of the Product life cycle are as following:

| | Stages → | Introduction | Growth | Maturity | Decline |
|---|---|---|---|---|---|
| 1. | **Sales** | Low sales | Rapidly increasing sales | Peak sales | Declining sales |
| 2. | **Costs** | High cost per customer | Average cost per customer | Low cost per customer | Low cost per customer |
| 3. | **Profits** | Negative | More profit | High profit | Declining Profit |
| 4. | **Customer adopters** | Innovators majority | Early Laggards | Early + late majority | |
| 5. | **Competitor** | Few | More in number | Stable number, beginning to decline | Declining numbers. |

In practice, a product sells slowly in the beginning. Barked by sales promotion strategies over period its sales pick up. In the due course of time the peak sale is reached. After that point the sales begins to decline. After sometime, the product loses its demand and dies. This is natural death of a product. Thus, every product passes through its life cycle. The product life cycle has been divided into the following four stages: Introduction, Growth, Maturity and Decline.

4. **Technical Analysis.** Technical analysis implies the adequacy of the proposed plant and equipment to prescribed norms. It should be ensured whether the required know-how is available with the entrepreneur. The following inputs concerned in the project should also be taken into consideration.

- Availability of land and site

- Availability of water power, transport, communication facilities.
- Availability of servicing facilities like machine shop, electric repair shop etc.
- Coping with anti-pollution law
- Availability of work force
- Availability of required raw material as per requirement in terms of quantity and quality.

5. **Management Competence.** Management ability or competence plays an important role in making an enterprise a success. In the absence of managerial competence the project which is otherwise feasible may fail. On the contrary, even a poor project may become a successful one with good managerial ability. Hence, while doing project appraisal, the managerial competence or talent of the promoter(s) should be taken into consideration.
6. **Ecological Analysis.** In recent years, environmental concerns have assumed great deal of significance. Ecological analysis should also be done particularly for major projects which have significant implication like power plant and irrigation schemes, and environmental pollution industries like bulk-drugs, chemical and leather processing. The key factors considered for ecological analysis are:
   - Environmental damage
   - Restoration measure

## 13.9 MARKET FEASIBILITY STUDY

Market feasibility analysis is the first stage in the process of project development. The purpose of the analysis is to examine the desirability of investing in pre-investment studies. For this purpose it is essential to examine project idea in the light of the available internal (inputs, resources & outputs) and external constraints (environment). When a project idea is taken up for developmental three situations can arise.

(i) The project may appear to be feasible,

(ii) Project may turn out to be not feasible or

(iii) The available data may not be adequate for arriving at reasonable decision regarding further investment.

In the last mentioned case, investment in pre-investment studies will obviously have to be adequate for arriving at reasonable decision regarding further investment and also have to be deferred till such times adequate data regarding the project feasibility is available. The project sponsoring body will therefore have to invest in collection additional data and refer the investment decision for the time being. In the second situation when the project is found to be not feasible, further investment in the project idea is completely ruled out. In the third situation, when the project idea is found to be feasible, the decision-makers can proceed to invest further resources in pre-investment studies and design development. The principle objectives of such study are to determine whether.

- The investment opportunity is so promising that an investment decision can be taken on the basis of information elaborated at the pre-feasibility stage.
- The project concept justifies a detailed analysis by pre-feasibility study.

- Any aspects of the project are crucial to its feasibility and necessitate in-depth investigation through function or a support studies such as market surveys, lab test, pilot study plan.
- The information is adequate to decide that the project is not either a viable preposition or attractive enough for a particular investor or investor group.

## 13.10 TECHNICAL FEASIBILITY STUDY

Techno-economic analysis is primarily concerned with the identification of project demand potential and the selection of the optimal technology which can be used to achieve the project objectives. The analysis provides necessary material on which the project design can be based. It also indicates whether the economy is in position to abserve the output of the project or not.

The examination of this aspect requires a thorough assessment of the various requirements of the actual production process and includes a detailed estimate of the goods and services needed for the project. So, the feasibility report should give a description of the project in terms of technology to be used, requirement of equipment, labour and other inputs.

Location of the project should be given special attention in relevance to technical feasibility. Another important feature of technical feasibility relates the types of technology to be adopted for the project. The exercise of technical feasibility is not done in isolation. The scheme has also to be viewed from economic considerations; otherwise, it may not be a practical proportion, however, sound technically may be:

- The promoter of the project can approach the problem of preparation of technical feasibility studies.
- Undertake a preliminary study of technical requirements to have a quick evaluation.
- If preliminary investigation indicate favorable prospects working out further details of the project. The exercise begins with engineering and technical specifications and covers the requirements of the proposed project as to quality, quantity and specification type of components of plant and machinery, accessories, raw materials, labour fuel, power, water, effluent disposal transportation, etc.

Thus, the technical feasibility analysis is an attempt to study the project basically from a technician's angle. The main aspects to be considered under this study are: technology of the project, size of the plant, location of the project, pollution caused by the project production capacity of the project, strength of the project. Emergency or stand-by facilities required by the project sophistication such as automation, mechanical handling, etc. required collaboration agreements, production inputs and implementation of the project are also to be studied.

## 13.11 FINANCIAL FEASIBILITY STUDY

The objectives of financial analysis are to develop the project from the financial angle and to identify these characteristics. Financial analysis concerns itself with the estimation of the project costs, estimation of project funds requirements. It also involves appraisal of the financial characteristics of the project so as to establish

the relative merits and demerits of the project as compared to other investment opportunities.

Financial analysis reduces investment proposition in diverse fields of human activity to one common scale, thereby simplifying the project is developing project financial forecasts.

## 13.12 SOCIAL FEASIBILITY STUDY

A project is may cross all the above barriers mentioned above and may found very suitable but is will lose its entire creditability, if it has no social acceptance. Though the social customs, conventions such as caste, community, regional influence etc,. are creating hindrances for development of a project should avoid all such social conflicts which will stand on the successful implementation of the project, for *e.g.*, considering the interests of the general public; projects which offer large employment potential, which channelize the income from less developed areas will stimulate small industries. In a nut shell, the feasibility report should highlight on these testing stones before it can be declared as complete and only after judging through these indicators a project can be declared as viable and can be submitted for finance or any other assistance from any institutions.

## 13.13 FORMAT OF FEASIBILITY REPORT

The sketch of feasibility report of the project covers the following:

1. Introduction
2. Summary and recommendations
3. Project capacity, chemistry of the product, specifications, properties, application and uses.
4. Market potential
5. Process and know-how
6. Plant and machinery
7. Location of the unit
8. Plot plan and building
9. Raw materials availability
10. Utilities, requirements
11. Effluents treatment
12. Personnel requirement
13. Capital cost
14. Working capital
15. Mode of finance
16. Manufacturing cost
17. Financial analysis
18. Implementation schedule

## REVIEW QUESTIONS

1. What is the meaning and definition project report? Explain the seed and significance of project report.
2. Explain the different contents and formulation of a project report.
3. What do you meant by network analysis?
4. Explain the most common errors of project report.
5. Define the project appraisal with suitable example.
6. Explain the following:
   (a) Market feasibility study.
   (b) Technical feasibility study.
   (c) Financial feasibility study.
   (d) Social feasibility study.

# 14. Project Identification and Formulation

## Chapter Outline

- Introduction
- Meaning of Project
- Features of Project
- Project Classification
- Life Cycle of a Project
- Project Identification
  - ⇒ Sources of Project Ideas
  - ⇒ Purpose and Need for Project Identification
  - ⇒ Steps in Project Identification
  - ⇒ Project Identification for an Existing Company
- Project Selection
- Scanning of Business Environment and Identifying Projects
- Project Formulation
- Steps in Project Formulation
- Project Evaluations

## 14.1 INTRODUCTION

In practice, an entrepreneur takes numerous decisions to convert his business idea into a running concern. The selection of right project goes to validate the right proposition: "*Well begun is half done*". An entrepreneur has an infinitely wide choice with respect to his project in different dimensions such as product/service, market, technology, equipment, scale of production, time phasing and location. In this chapter, we will study how an entrepreneur identifies and selects a right project product for his enterprise and concerned with investigating and screening of project ideas, steps in the project identification process and also consideration involved in identifying the new projects by an existing company.

## 14.2 MEANING OF PROJECT

A project is generally defined as a program of work to bring about a beneficial change and which has:

- A start and an end,
- A multi-disciplinary team brought together for the project,
- Constraints of cost, time and quality,
- A scope of work that is unique and involves uncertainty.

Project can be defined as follows:

**Important Point:** *"A project typically has a distinct mission that it is designed to achieve and a clear termination point, the achievement of the mission".* *-Newman et.al*

*"Project is the whole complex of activities involved in using resources to gain benefits".* *-Gillinger*

*"A project is an organized unit dedicated to the attainment of goal-the successful completion of a development project on time, within budget, in conformance with pre-determined program me specification".* *- According to Encyclopedia*

## 14.3 CHARACTERISTICS OF PROJECT

A project has following features:

1. **Objectives:** A project has a set of objectives, goals or a mission. Once the objectives are achieved the project is treated as completed.
2. **Life Cycle:** A project has a life cycle. The life cycle consists of five stages, *i.e.*
   (a) Conception stage,
   (b) Definition stage,
   (c) Planning and organizing stage,
   (d) Implementation stage and
   (e) Commissioning stage.
3. **Uniqueness and Team Work:** Every project is unique and any two projects cannot be similar for example: Setting up a cement plant and construction of a highway are two different projects having unique features.

   Project is a team work and it normally consists of diverse areas. There will be specialized personnel in their respective areas and co-ordination among the diverse areas calls for team work.
4. **Complexity, Risk and Uncertainty:** A project is a complex set of activities relating to diverse areas. Risk and uncertainty go hand in hand with project. A risk-free, it only means that the element is not apparently visible on the surface and it will be hidden underneath.

   A high level of work in a project is done through contractors. The more the complexity of the project, the more will be the extent of contracting.
5. **Customer Specific Nature:** A project is always customer specific. It is the duty of any organization to go for a products or services that satisfies customer needs.
6. **Unity in Diversity:** A project is a complex set of thousands of varieties. The varieties are in terms of technology, equipment and materials, machinery and people, work, culture and others.

## 14.4 PROJECT CLASSIFICATION

Project classification helps in expressing and highlighting the essential features of project. The major classifications of project are as shown in Fig. 14.1:

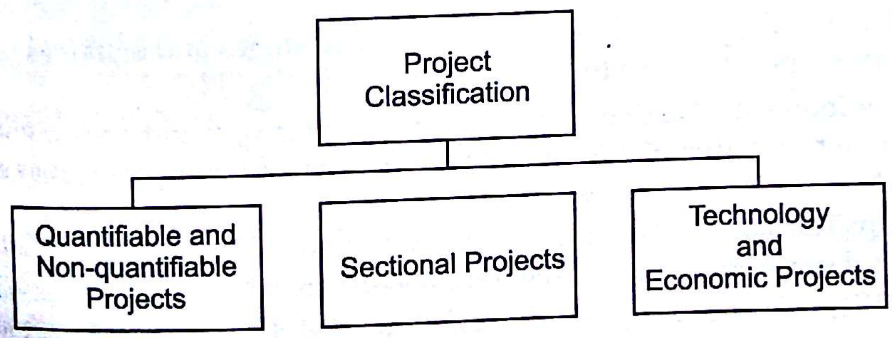


**Fig. 14.1** Project Classification

1. **Quantifiable and Non-Quantifiable Projects:** Projects related to power generation, mineral development, industrial development are examples of quantifiable projects. In these projects a right quantitative assessment of benefits can be made and termed as quantifiable projects.
   Projects involving health, education and defense are some examples of non-quantifiable project. In these projects which quantitative assessment cannot be made are termed as non-quantifiable projects.
2. **Sectional Projects:** Projects classification is based on different sectors. Some examples are:
   - Industry and mining sector
   - Information technology sector
   - Agriculture and allied sector
   - Irrigation and power sector
   - Transport and communication sector
   - Miscellaneous

   This system of classification has been found useful in resource allocation at macro level.
3. **Technology- Economic Projects:** Projects can also be classified on the basis of techno-economic characteristics. This type of classification includes factors intensity-oriented classification, causation oriented classification as discussed below.
   (i) **Factor Intensity-oriented classification:** This is based on intensity of factors. Projects may be classified as capital intensive or labour intensive. If a large investment is made in plant and machinery then such projects are called capital intensive. On the other hand if involves large number of human resources it will be termed as labour intensive.
   (ii) **Causation-oriented classification:** Projects can be classified as demand based or raw material based projects. The existence of demand makes it a demand based project whereas availability of raw material, skills and other inputs makes it raw material based.
   (iii) **Magnitude-oriented classification:** This is based on the size of investment involved in the projects, accordingly project are classified into large scale, medium-scale or small-scale projects.

## 14.5 LIFE CYCLE OF A PROJECT

A typical methodology would involve a number of stages and activities which occur at different parts of the life cycle as shown in Fig. 14.2.

1. **Preparation:** This stage involves the project manager and sponsor in the preparation and approval of an outline project justification, plan and project budget.
2. **Start up:** The startup stage involves the selection and briefing of the project team and some discussion on the roles and organization.
3. **Feasibility or research stage:** This stage will establish whether the project is feasible and establish the risks and key success measures. Unless the organization undertakes research or new product development, feasibility

often means - 'Can this process or technology be cost effectively applied to the organization or department', rather than: 'is it generally feasible?'

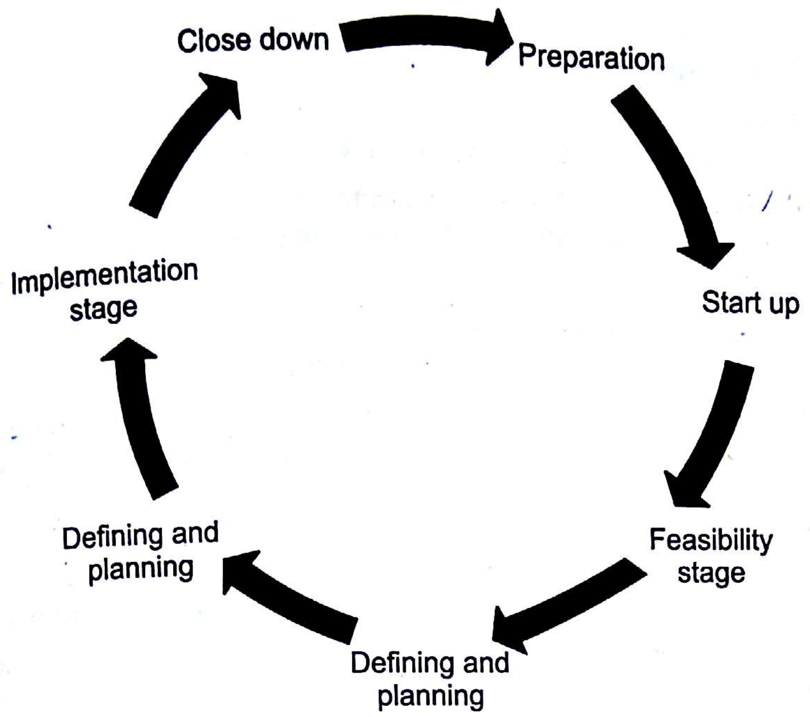


Fig. 14.2 Life Cycle of a Project

4. **Defining and Planning**: The project should be in more detail by writing and publishing a full definition of the project and determining a project plan. This work is undertaken by the team and co-ordinated by the project manager.
5. **Implementation stage**: It involves the execution of the project as approved, whilst carefully monitoring progress and managing changes. The team may need to be expanded at this stage to resource all the tasks. If so, it is essential they are fully briefed and feel 'included' as part of the team *i.e.* there must be sense of belongingness.
6. **Close down**: This stage involves the satisfactory delivery of the products or services that achieve the beneficial gain.

## 14.6 PROJECT IDENTIFICATION

This section provides a brief summary of the main issues of the project identification phase, which takes place before the preparation and procurement phases. The project identification phase is important because it determines whether the selected project can be delivered. Project selection process starts with the generation of a product idea. The project ideas can be discovered from various internal and external sources. They may be as under:

1. Knowledge of potential customer needs.
2. Watching emerging trends in demand for certain products.
3. Scope for producing substitute product.
4. Going through certain professional magazines catering to specific interest like electronics, computers, etc.

5. Success stories of known entrepreneurs or friends or relatives.
6. A new product introduced by the competitor.

Project identification is concerned with collection, compilation and analysis of economic data for the eventual purpose of locating possible opportunities for investment and with the development of such opportunities.

Opportunities according to Peter Drucker are of three kinds:

1. **Additive opportunities:** Those which enables optimum utilization of existing resources without any changes in character of business. These opportunities involve minimum disturbance to the existing state of affairs and hence holds least risk.
2. **Complementary opportunities:** It involves the introduction of new ideas and lead to certain amount of change in the existing structure.
3. **Breakthrough:** These opportunities on the other hand involve fundamental changes in both the structure and the character of business.

### 14.6.1 Sources of Project Ideas

Project ideas could originate from the various sources as mentioned below:

- Success story of a friend/relatives
- Experience of others in manufacture/scale of product
- Examining the inputs and outputs of industries
- Plan outlays and government guidelines
- Suggestions of financial institutions and developmental agencies
- Investigation of local materials and resources
- Economic and social trend of the economy
- New technological developments
- Project profiles and industrial potential surveys
- Visits to trade fairs
- Unfulfilled psychological needs
- Possibility of reviving sick units

### 14.6.2 Purpose and Need for Project Identification

The entire economic management planning is based on two fundamental assumptions, *i.e.*

- Limited means
- Unlimited ends

Identification and selection of a project is a scientific process. This process is based on certain essential conditions. It may differ from project to project. The essential conditions which should be taken into consideration for identification and selection of production projects are as follows:

1. Project should be in conformity with the economic needs of the area.
2. It should take into account the depriving factors which might have adverse impact.
3. The input-output ratio should be optimum.

4. The purpose of the project is to increase the production and generate employment in the area.
5. Thus, the above said conditions will differ due to resources availability, use pattern and other relevant conditions of the area. Besides that, project should also consider certain national priorities.

### 14.6.3 Steps in Project Identification

Project ideas are like other ideas which do not take concrete shape immediately. There are several stages of making propositions their considerations and scrutiny for their soundness. An idea is first born, it is under consideration for sometimes and subsequently it begins to take some definite shape. The project ideas to develop take almost the same course. This project identification may be broadly divided into four stages as shown in Fig. 14.3.

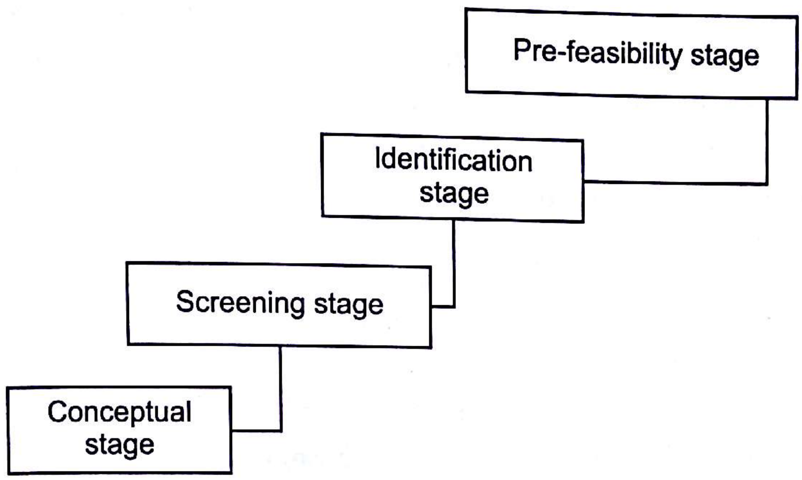


Fig. 14.3 Steps in Project Identification

1. **Conceptual stage**: This stage is from where project ideas are generated. A number of project ideas may be generated either by those officials or non-officials and entrepreneurs individually or collectively who are acquainted and familiar with the area.
2. **Screening stage**: At which unviable ideas are eliminated. In the second stage, project ideas generated above are screened and preliminary exercise to weed out the bad or unviable ideas.
3. **Identification stage**: At which viable projects are selected. This study is necessarily preliminary and the broad one and has a limited objective of providing planners with a choice of projects from which they can make a selection.
4. **Pre-feasibility stage**: At which pre-feasibility studies are taking up. Pre-feasibility study and these can be differentiated opportunity study and a detailed feasibility study and these can be differentiated mainly on the basis of information required for respective stages.

### 14.6.4 Project Identification for an Existing Company

Existing company's essentially large scale company forms of organizations are continuously developing various projects for their developmental purposes. An

existing company which seeks to identify new project opportunities should undertake a "SWOT" analysis. It is an acronym law of strengths, weakness, opportunities and threats. This analysis evaluates all these four characteristics of existing company. A brief summary of the points required for SWOT analysis is given below:

1. Availability of internal financial reasons for new projects after taking into account the need for replacement expenditure, increase in working capital, repayments of loans and dividend payments.
2. Capability of top management of the company.
3. State of industrial relations in the company.
4. Capability of raising external financial resources.
5. Availability of production facilities.
6. Technological capabilities of the company.
7. Availability of different sources of raw materials and its utilization.
8. Availability of infrastructural facilities.
9. Cost structure and profit margins of the company.
10. Distribution network of the company.
11. Market share of the company.
12. Impact of corporate laws.
13. Likely changes in the governmental policies.
14. Possibility of evolving new technology and its impact on the cost structure of the company.
15. Existence and severity of competition.
16. Changes in the customers preferences, fashion, tastes, etc.

## 14.7 PROJECT SELECTION

Identification of a new project is a complex problem. Project selection process starts with the generation of project ideas. In order to select the most promising project, the entrepreneur needs to generate a few ideas about the possible project one can undertake. It starts from where project identification ends and these are analyzed in the light of existing economic conditions, the government policy and so on. For this purpose a tool is generated used what is called 'SWOT analysis'. On the basis of this analysis, the most suitable idea is finally selected to convert it into an enterprise.

**Project selection involves following steps:**

1. **SWOT Analysis:** It has always been important for a business to know and understand how it fits in and interacts with the surrounding environment. The internal like office, factory, shop environment, etc. and external view that how your business operates with the outside world. Researching your environment will benefit the management team by putting you in a position to develop a strategy for both the long and short term. Recognizing the strengths and weaknesses before tackling the opportunities and threats is the best way to approach the analysis: the more strengths and opportunities the better they can both be seen as the bigger influences for the success of your company. These are as following:

(i) **Strengths:** The strengths can be considered as anything that is favorable towards the business for example:

1. Currently in a good financial position (few debts, etc.)
2. Latest machinery installed.
3. Skilled workforce (little training required).
4. Company name recognized on a National/Regional/Local level.

(ii) **Weaknesses:** Recognizing the weaknesses will require honest and realistic that does not leave anything out as this is an important part as to realize what needs to be done to minimize this list in the future. Here are a few examples:

1. Currently in a poor financial position (Large debts, etc.)
2. Un-Skilled employees (Training required)
3. Machinery not up to date (Inefficient)
4. Rented premises (Adding to costs)
5. Poor location for business needs (Lack of visibility, transport links etc.)

(iii) **Opportunities.** SWOT Analysis can now influence the opportunities for the business. These can be seen as targets to achieve and exploit in the future for example:

1. Good financial position creating a good reputation for future bank loans and borrowings.
2. Skilled employees means that they can be moved and trained into other areas of the business.
3. Competitor going bankrupt (Takeover opportunity).
4. Broadband technology has been installed in the area (useful for Internet users).
5. Increased spending power in the Local/National economy.
6. Moving a product into a new market sector.

(iv) **Threats:** The final part of the analysis will also be seen as the most feared- the threats. It has to be done and therefore taking into account what you have listed as your weaknesses, the threats will now all seem too clear. Examples are:

1. Large and increasing competition.
2. Rising cost of Wages (Basic wage, etc.).
3. Possible relocation costs due to poor location currently held.
4. Local authority refusing plans for future building expansion.
5. Increasing interest rates (increases borrowing repayments, etc.).
6. End of season approaching (if you depend on hot weather, etc.).

Once the SWOT analysis is complete now this is the time to put it all together and look closely to form a strategy. This may well depend on your companies original objectives and goals but the whole process will certainly give an overall look at the current position of your business. It involves how you can exploit the opportunities and how to eliminate or deal with the threats.

2. **Technical, economic and financial soundness:** Project ideas identified earlier are screened on the basis of their technical, economic and financial soundness.

After screening, the ideas are translated into project profiles. A project profile consists of the following broad items.

1. Economic size.
2. Status of industry or scope and raw material availability.
3. Cost of production and capital cost.
4. Utility requirements and infrastructure facilities needed.
5. Profitability.
6. Government policy.

## 14.8 SCANNING OF BUSINESS ENVIRONMENT AND IDENTIFYING PROJECTS

In the preceding stage, the primary objective was to ensure that no worthwhile idea would be ignored by the entrepreneur. However, the conversion of a basic idea into a viable project requires rigorous analysis and detailed planning. It would be impossible for us to submit a large number of proposals to such an exercise. Hence, the need arises for a preliminary screening of feeble ideas to eliminate *i.e.*, those project ideas which are not primafacie promising. The following factors may be used as Screening Devices to eliminate such alternatives:

1. **Organization Strengths and Weaknesses**: Project ideas must be compatible with the organization. A project idea which falls in the area of an organization's strength can be converted into an effective project. A project idea, however profitable basically, which falls in the area of a company's weaknesses cannot be converted into a successful project.
2. **Adequate Market**: Every business organization requires a minimum level of business (Break Even Point- no profit no loss point) to be viable. Where the market is restricted and cannot allow the organization to reach the break even point (BEP) in the near future, the prospects of success are rather limited.
3. **Availability of Infrastructure**: No business venture can succeed in the absence of basic support/services like transportation, electricity, water supply, etc. In most of the cases, the business organization cannot create these services independently. The absence of these facilities would trouble the project from inception.
4. **Availability of Essential Inputs and Labour**: The entrepreneur must consider whether there is a regular and assured supply of essential inputs and labour to ensure regularity of operations essential for success of the venture.
5. **Cost Constraints**: If the estimated cost of producing the product/service is comparatively very high in view of factors like high material costs or labour costs or any related reasons, the project idea should be eliminated.
6. **Risk Consideration**: Risk levels associated with various projects differ on the basis of factors like changes in technology, changes in fashion, and vulnerability to trade cycles. Only well established and cash - rich organizations can undertake such projects.

## 14.9 PROJECT FORMULATION

Project formulation is a process whereby the entrepreneur makes an objective and independent assessment of various aspects of an investment proposition of a project idea for determining its total impact and also its liability. This forms an important stage in the pre-investment phase that is the period from the conception of an idea until the final analysis to decide about the future of the project idea. This makes it an analytical management aid. The aim of project formulation is to achieve the project objectives with the minimum expenditure and adequate resources.

## 14.10 STEPS IN PROJECT FORMULATION

The different steps of project formulation process are briefly describes as follows as shown in Fig. 14.4.

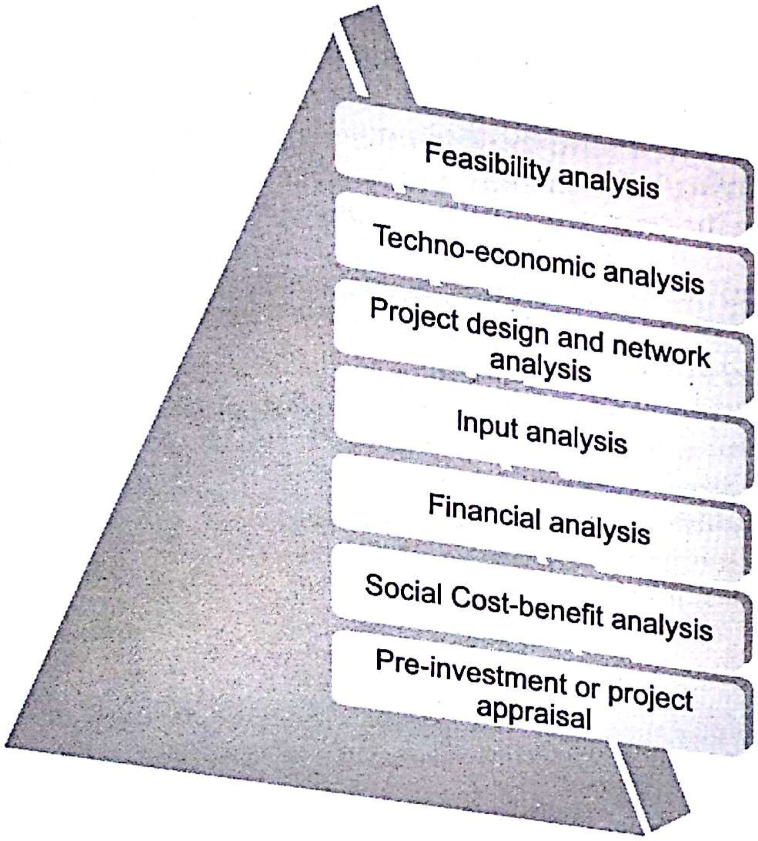


**Fig. 14.4** Steps in Project Formulation

1. **Feasibility analysis**: Feasibility analysis is the first stages in the process of project development. The purpose of the analysis is to examine the desirability of investing in pre-investment studies.
2. **Techno-economic analysis**: Techno-economic analysis provides necessary material on which the project design can be based. It also indicates whether the economy is in position to absorb the output of the project or not.
3. **Project design and network analysis**: It identifies the flow of events, which must take place before a project can start yielding the results for which it has been set up. The inter-relationship between various activities of a project in most conveniently expressed in the form of a network diagram *i.e.*, Critical

Path Method (CPM) and Project Evaluation and Review Technique (PERT). Project design and network analysis are concerned primarily with the development of the detailed work plans of the project and its time profile, and the presentation of this plan is form of a detailed network drawing.

4. **Input analysis:** The objective is to identify and quantify the project inputs and to assess the feasibility of a sustained supply of these inputs all through the effective life span of the project.
5. **Financial analysis:** The objective of financial analysis is to develop the project from the financial angle and to identify these characteristics. Financial analysis concerns itself with the estimation of the project costs, estimation of project funds requirements, working capital, cash flow, net present value (NPV), internal rate of return (IRR).
6. **Social Cost- benefits analysis:** In judging the overall value of the project, the effect of the project on society as a whole is very essential. While financial analysis evaluates a project from the profitability point of view, social cost benefit analysis views it from the point of view of national viability.
7. **Pre-investment or project appraisal:** Pre-investment appraisal presents the project idea in a form in which the project sponsoring body, the project implementing body and the outside agencies can take investment decision regarding the proposals.

## Review Questions

1. What do you mean by project formulation? Explain the several aspects of project formulation.
2. What factors would you take into account for identifying promising investment opportunities?
3. What is SWOT analysis and how it can be done?
4. Explain the process of project identification.
5. What are the different phases of project formulation?
6. Explain the criterion to be adopted while formulating a project.
7. "Formulation of projects involves scientific procedure" elucidate.

# 15... International Entrepreneurship Opportunities

## Chapter Outline



## 15.1 INTRODUCTION

As more countries become market oriented and developed the distinction between foreign and domestic markets is becoming less pronounced. International business has become increasingly important to firms of all sizes. The successful entrepreneur will be someone who understands how international business differs from domestic business and is able to act accordingly.

## 15.2 MEANING AND DEFINITION

International entrepreneurship is the process of an entrepreneur conducting business activity across and beyond the national boundaries. It may consist of exporting, licensing, opening sales office in another country etc.

**Important Point:** *"International entrepreneurship is defined as development of international new ventures or start lips that from their inception engage in international business, thus viewing their operation domain as international from the initial stages of international operations".*

## 15.3 NATURE OF INTERNATIONAL ENTREPRENEURSHIP

The companies which are incurring high level of fixed costs can lower their manufacturing costs by spreading these fixed costs over long number of units by selling their products in global market. The international entrepreneurship natures are shown in Fig. 15.1

1. **Sell their products in foreign market:** Entrepreneur can sell their products in foreign market which have reached the maturity stage of their life cycle in domestic markets and earn profit by their sales. International entrepreneurship is beneficial as if sales of company are declining in domestic market, they can

sell their products in the international market considering demand for product in other country market customers.

2. **Cultivate habit:** Internationalization of business will teach entrepreneurs, how to cultivate habit of customer relation management (CRM).

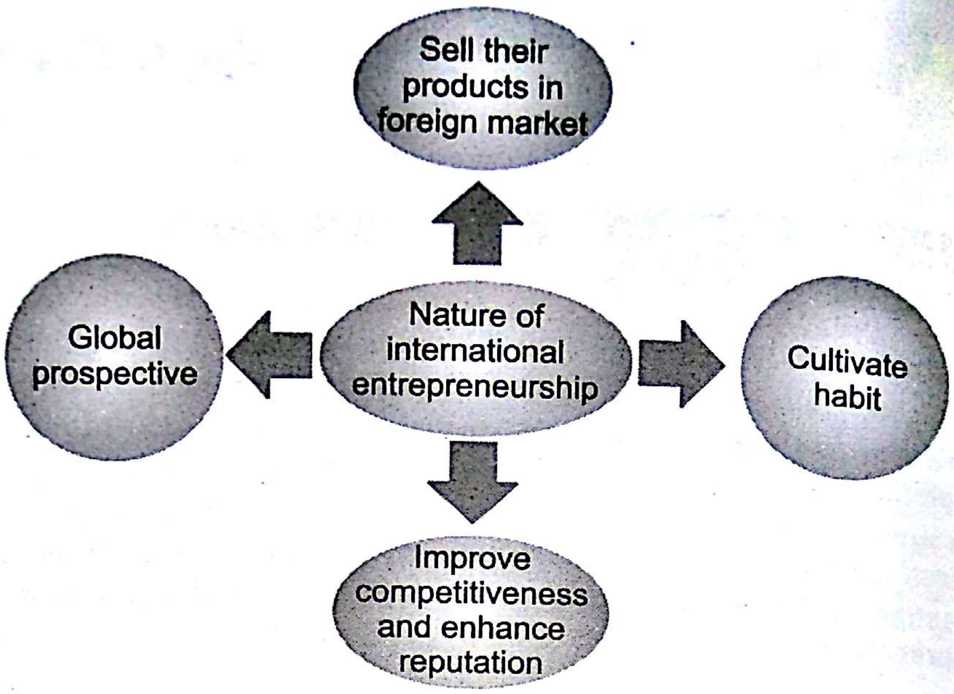


**Fig. 15.1** Nature of International Entrepreneurship

3. **Improve competitiveness and enhance reputation:** Entrepreneur in process of satisfying foreign customers have to produce product as per their requirements and quality expectation by which entrepreneur will not only produce quality product in international market but also in national market. Entrepreneur can improve their entrepreneurial competitiveness and enhance reputation.

4. **Global prospective:** Entrepreneurs can hire motivated, multi-lingual employees to learn constantly about the foreign markets. They will think globally and start developing an outlook from a global prospective. Being global will make the entrepreneur sensitive towards their customers - domestic, adopt more respectful attitude towards foreign habits and customers.

## 15.4 IMPORTANCE OF INTERNATIONAL BUSINESS TO FIRM

International business is a term used rarely to describe all commercial transactions that take place between two or more regions, countries and nations beyond their political boundary. Usually, private companies undertake such transactions for profit and governments undertake them for profit and for political reasons. It refers to all those business activities which involve cross border transactions of goods, services, resources between two or more nations. Transaction of economic resources includes capital, skills, people etc. The importance of international business firm is:

1. **Lower manufacturing cost:** If the company manufacturing cost increases by manufacturing product in home country, than company has an alternative for production process in host country, on the contrary if the company is in no profit or no loss situation than company can choose in any option.

2. **Growth opportunity:** An entrepreneur whose core business strategy is expansion and diversification of business, international business is one of the primary platform to achieve these objectives.
3. **Increased sales and profit:** When the entrepreneurs are not able to earn profit or demand for their product declines in local market they can choose to sell their products in foreign market where life cycle of product is in favourable condition.
4. **Advantage of inexpensive labour:** Quantity and Quality of labour is one of the major challenge for every business, if the labour is cheap in foreign countries than company can outsource required labour if organization is into foreign operations.
5. **Utilization of talent and managerial competence:** When business are not able to get required talented work force in country, they can get the activity outsourced or hire host country employee which has given birth to concept of expatriation.
6. **Globalization of customers:** It refers to when customers in country prefer purchasing foreign brand products than domestic companies have to go in for internationalization of business to keep in pace with competition to attract customers. Tata international begin to operate in international market after entry of foreign competitors in Indian market like ford.
7. **Expansion of domestic market:** International business causes domestic market to expand beyond national boundaries. When the domestic market gets fully tapped than company has an option to go in for expansion of business to market their products in international market.
8. **Pay-offs of international business:** International business improves image of the company in domestic market and attracts more customers in domestic market due to internationalization of business.
9. **Globalization of competitors:** International business increases the opportunity not only for the survival and growth but also motivates companies to face competition from global entrants in market, which in turn leads to growth of market, pursuing global scale efficiencies etc.

## 15.5 DOMESTICS vs INTERNATIONAL ENTREPRENEURSHIP

Whether domestic or international, an entrepreneur about the same basic issues is concerned sales, costs and profits. What varies is the relative importance of the factors being considered. International entrepreneurial decisions are more complex due to uncontrollable factors such as the following:

| S. No. | Domestics Entrepreneurship | International Entrepreneurship |
|---|---|---|
| 1 | When an entrepreneur is operating in national level he is required to understand economic conditions with in country | But at an international level he should be having information about economic system of countries where he wants to run business which includes currency rate, phase of business cycle etc. |

| | | |
|---|---|---|
| 2 | When entrepreneur is operating at domestic level he should focus on development state of domestic country. | But when he operating on international scale he has to view country from developed, developing and underdeveloped perspective and accordingly plan in business strategies in economy. |
| 3 | Entrepreneur operating at national level should understand cultural issues persisting in home country. | In international level he has to understand and manage cultural diversity of customers as well as employees in company. |

Politics and laws play a critical role in international business as well as in domestic business. Entrepreneur should be aware about political and legal environment in the domestic as well as international market. Entrepreneur going in for internationalization of business have to study domestic as well as international policy, as restriction laid in home country for export of goods affect trade of entrepreneur and restriction in host country on entering of new entrepreneurs in their company.

## 15.6 STAGES OF ECONOMIC DEVELOPMENT

The processes of the stage of economics development are shown in Fig. 15.2

1. **Traditional society stage:** Every economy begins with traditional society which is characterized with low per capita income and low degree of technical know-how.

   *Feature of Traditional society*

   - Science and technology develop at very slow phase in economy.
   - Political power in society remains concentrated with dominant social groups in society.
   - People in country believe more in family, culture, customs, religion and caste system which leads to problem of lack of mobility of labour which hinders employee growth in country.
   - Country is more or less dependent of agriculture for development in country.

2. **Pre conditions of take-off stage:** In this stage of economy conditions are created conductive of growth. In this stage entrepreneurs start thinking in terms of modernization, capital formation and profit oriented ventures.

   *Features of Pre-conditions of take-off stage*

   - Focus towards foreign trade
   - Citizens of country give more importance on developing personal skills in order to face competition in country.
   - Decline in birth rate.
   - Part of government revenue is imparted towards infrastructure development in country.

- People start giving importance to national and international developments then merely confining them to social issues.
- Less dependence on agriculture.

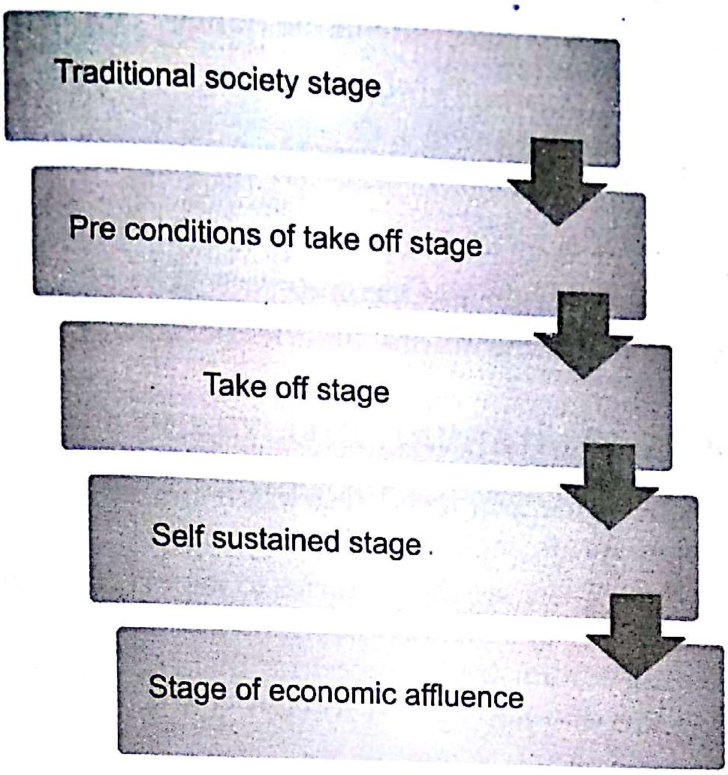


Fig. 15.2 Stage of economics development

3. **Take off stage**: In this stage economy is no more dependent on other countries and is self sustaining in this stage. Economy can progress without any external support from other countries.

   *Features of Take off stage*

   - Increase in demand for products by consumers in market.
   - Development of various sectors for example-primary, secondary and tertiary sector takes place in the country.
   - Re-investment of profit.
   - Political stability in country indirectly leads to growth in industrial sector in country creating favourable condition for trade in country.
   - Social framework improves as citizens than being bonded with family focus on moving to places for career growth and development.

4. **Self sustained stage**: This stage can be defined as stage in which an economy demonstrates the capacity to move beyond the original industries which provide the take off and to apply efficiency over its worldwide range of resources.

   *Features of Sustained stage*

   - Dependencies on other countries are considerably reduced.
   - New political as well as social institution is established in country.
   - Modern techniques are used during the process of production in country.

- A condition of employment improves and reduces dependency o agriculture.
- Rise in the rate of investment in the country.

5. **Stage of economic affluence:** In this stage as consumer's other then dail consumption products prefers purchasing durable products.

   ***Features of Stage of economic affluence***

   - Standard of living in country increases as result of development of facilities in country.
   - Country in this stage starts spending more on military forces.
   - Increase in production and income.
   - Consumption of comforts and luxuries become a common feature.

## 15.7 BARRIERS TO INTERNATIONAL TRADE

Trade barriers are government-induced restrictions on international trade. The barriers can take many forms, including the following:

1. **Non tariff barriers:** These are the obstacles to imports other than tariffs such as testing, certification, or bureaucratic hurdles that have effect of restricting imports. These are administrative measures that are imposed by a domestic government to discriminate against foreign goods and in favour of home goods.
2. **Tariff barriers:** Tariff means duty levied by the government on imports. Imposing tariff raises the price of imported goods making them expensive and less attractive to consumers to protects makers of comparable domestic products and services.
3. **Lack of information:** As entrepreneur is new entrant in international market he is unaware about the market conditions in host country and taste and preference of customers which may lead to issues in terms of acceptance and locating product in market.
4. **Financing problems:** As international business involves huge risk, financial institutions may be reluctant in terms of providing required finance to entrepreneurs.
5. **Attitude of entrepreneur:** When an entrepreneur has negative mindset that foreign market is unknown to him and he might find it difficult to set up his business in new country will prove to be a major barrier for international trade.
6. **Political barrier and cultural barriers:** In few country their exist abundant opportunity for business but political scenario in country will be instable such as kidnappings, bombings, violent against business and employees which proves to be major question mark in terms of future success of business. As entrepreneur is new entrant in host country he may not be aware about language, education, tradition, religion, values of citizens which will make it difficult for the entrepreneur to understand mindset, taste and preference of customer in market.
7. **Technical barriers:** Basically refers to before countries goods enter into foreign market it has to go through certain test for authentication. In Unites States, before food products from others is marketed it has to be tested for checking

## REVIEW QUESTIONS

1. What do you mean by International Entrepreneur ship? Explain the Nature of International Entrepreneurship.
2. Describe the importance of International Business to firm.
3. What are the difference between domestics and international entrepreneurship?
4. Explain the Stages of Economic Development and their features.
5. What are the main barriers to International Trade?

# 16 Family and Non-family Entrepreneur

## Chapter Outline



## 16.1 INTRODUCTION

Organizational culture is an important strategic resource that family firms can use to gain a competitive advantage. Entrepreneurship and the development of small and medium size businesses continue to be at the forefront of socio-economic development in virtually all economies today. Entrepreneurial led small business, provide social stability and serve as the engine of economic growth. Governments and policy makers have become aware of both the social and economic development benefits associated with entrepreneurship and small and entrepreneurship (SME) development.

## 16.2 PROFESSIONALISM

Professionalism is actually the process by which given occupation become professions in the sense of attaining professional status. That represents characteristic of a professional person.

### 16.2.1 Elements of Professionalism

The elements of professionalism are selfless accountability excellence honesty/ integrity dutiful respect to other as shown in Fig. 16.1.

1. **Unselfish**: This showing unselfish concern for the welfare of others.
2. **Excellence**: The knowledgeable skillful competency is to retrieve and handle information appropriate decision making skills and competency in skills of communication.
3. **Honesty/ integrity**: The quality of professional is being honest, moral soundness, undivided or unbroken.
4. **Dutiful**: The appreciation is of the role is aptitude for personal development and responsibility.
5. **Gaining & giving respect**: Any professional must gain the respect of others and appropriately respect others.

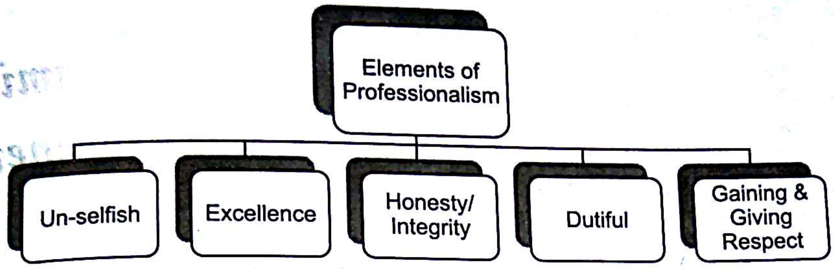


**Fig. 16.1** Elements of Professionalism

## 16.3 FAMILY ENTREPRENEUR

A family entrepreneurship is defined in terms of: Ownership control by members of a family, strategic influence of a family in the management of the firm and concern for family relationship regarding the dream of continuity across generation.

## 16.4 PROFESSIOANLISM vs. FAMILY ENTREPRENEURS

The professionalism and family entrepreneurs can be compare in following terms as shown in Fig. 16.1.

1. **Degree of open mindedness:** Professional is open minded, receptive to new ideas, ready to experiment and have quality of adaptability. While family entrepreneurs generally lack this.
2. **New practices:** Include quality certification, participative management, change in working style and financing pattern. Professionals are always leaders in adopting them and experimenting with them. Whereas, in family entrepreneurs such attitude is rarely found.

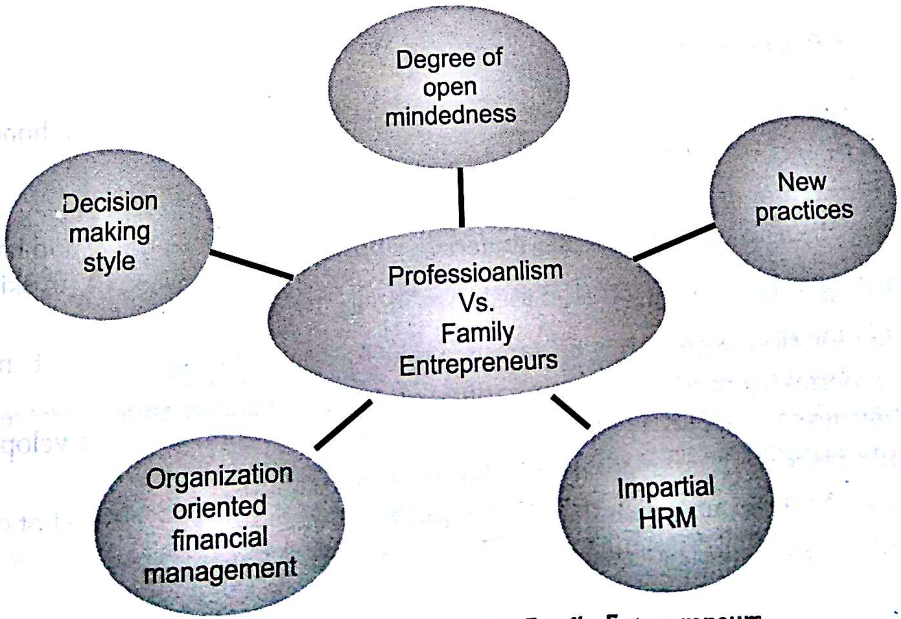


**Fig. 16.2** Professionalism Vs. Family Entrepreneurs

### 16.5.1 ▌Introduction

Women entrepreneurs may be defined as a woman or groups of women, w initiate, organize and run a business enterprise. In terms of Schumpeterian conc of innovative entrepreneurs, persons who innovate, initiate or adopt a busin activity are called business entrepreneur.

Based on innovation: "Women who innovate, imitate or adopt a busine activity are called women entrepreneurs".

### 16.5.2 ▌Functions of Women Entrepreneurs

The functions of women entrepreneurship for exploration of the prospects o starting a new business enterprise, undertaking a risk and handling of economi uncertainties involved in business. These are:

1. Determination of objectives.
2. Project preparation.
3. Product analysis.
4. Form of business.
5. Raising funds.
6. Procuring men, machine and materials.

According to Frederick Harbison as shown in Fig. 16.3:

1. Exploration of prospects of starting a new business enterprise.
2. Undertaking of risks and the handling of economic uncertainties involved in business.
3. Introduction of innovation or imitation of innovations.
4. Coordination, administration and control.
5. Supervision and leadership.

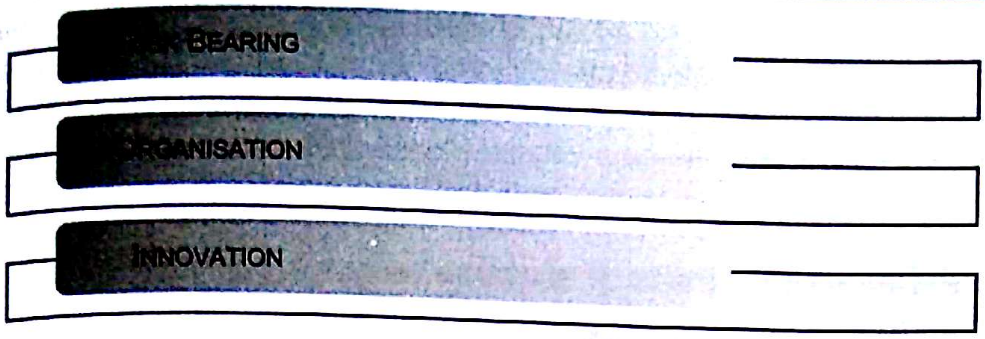


Fig. 16.3 Functions of Women Entrepreneurship

### 16.5.3 Role of women as an Entrepreneur's

The role of women as an Entrepreneur's imaginative attribute to work hard persistence ability and desire to take risk profit earning capacity as shown in Fig. 16.4.

1. **Imaginative:** It refers to the imaginative approach or original ideas with competitive market. Well-planned approach is needed to examine the existing situation and to identify the entrepreneurial opportunities. It further implies that women entrepreneur's have association with knowledgeable people and contracting the right organizational offering support and services.

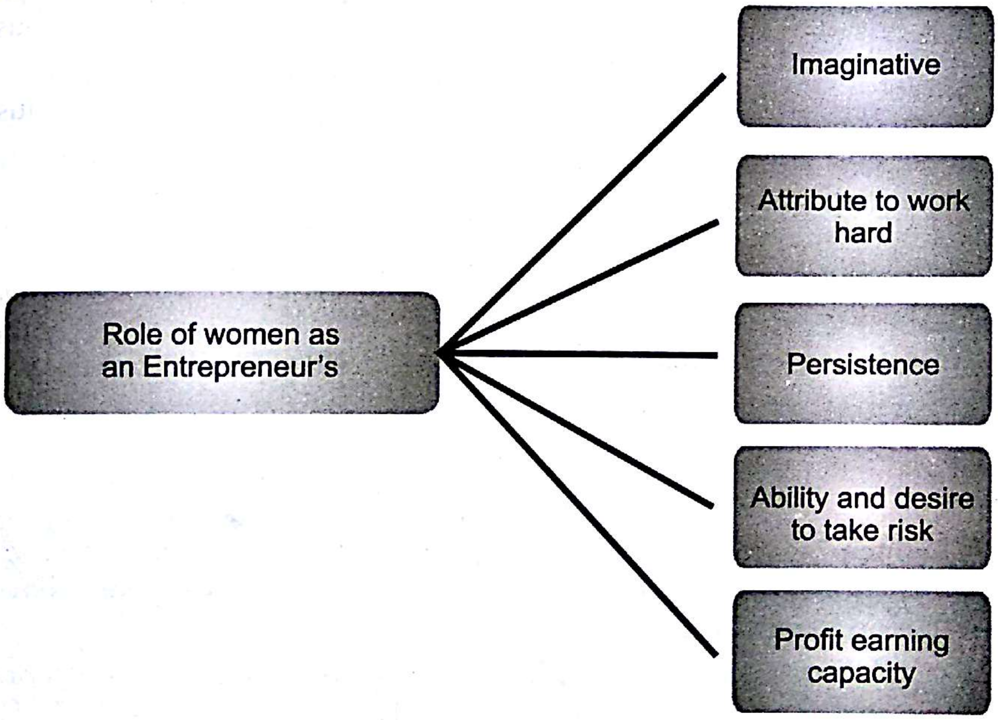


Fig. 16.4 Role of women as an Entrepreneur's

2. **Attribute to work hard:** Enterprising women have further ability to work hard. The imaginative ideas have to come to a fair play. Hard and smart work is needed to build up an enterprise.
3. **Persistence:** Persistence women entrepreneurs must have an intention to fulfill their dreams. They have to make a dream transferred into an idea enterprise; studies show that successful women work hard.

4. **Ability and desire to take risk:** In ability and desire to take risk, the desire refers to the willingness to take risk and ability to the proficiency in planning making forecast estimates and calculations.
5. **Profit earning capacity:** In profit earning capacity, she should have a capacity to get maximum return out of invested capital.

### 16.5.4 Leadership traits of successful entrepreneurs.

Successful entrepreneurs sharpen their character and leadership traits over time to keep reaching for new horizons and to achieve ever-shifting goals. Success, therefore, is a journey and not a destination. The following traits are required to work on to achieve sustainable success—

1. **Successful entrepreneurs gain the respect of their peers:** One of the most obvious characteristics of an exceptional entrepreneur is an equitable and unbiased temperament. Plain and simple, the successful entrepreneur recognizes that all are at par. With an attitude of respect for others, successful entrepreneurs gain respect from everyone they encounter. Strategies, attitudes and methods sort down to each person they work with. A successful entrepreneur always gives opportunity to everyone for growth.

   A wise entrepreneur is confident and good at trusting their own ideas and instincts. Successful entrepreneurship is underpinned by persistence, determination and a high level of self-discipline. Success is all about a strong code of ethics, a strong belief, desire and passion.
2. **Successful entrepreneurs follow a plan:** Haphazard plans do not work for entrepreneurs; no one reaches the destination without a map or a guide to follow. Most successful entrepreneurs start out by writing a basic business plan to guide their endeavours. It should short and simple which include marketing strategies, objectives, expectations, ideas and suitable strategy to handle the competition. A business plan should be reviewed and updated periodically.
3. **Successful entrepreneurs think differently and creatively:** Entrepreneurs think differently and creatively. Whether a business idea has already been tried makes no difference to entrepreneurs. They find better paths to do things and know that every idea can be expanded upon, made better, enhanced or broadened. Successful entrepreneurs are willing to think outside the proverbial box, which means using their imagination, experimenting out new things and expanding on a vision. When a strategy is not working, they move on to another approach or idea.
4. **Successful entrepreneurs explore their skills:** Successful entrepreneurs realize the strengths and weaknesses as well as a multitude of skills and talents. Successful people ask themselves often what skills they have that no one shares in exactly the similar way. Successful entrepreneurs explore their skills and they find the ones that match their ideas.
5. **Successful entrepreneurs visualize their success:** Successful entrepreneurs visualize their success. Intention is a powerful tool. Imagine what it will feel like when you have reached a particular set of goals. Get in touch with the feelings you have as a successful entrepreneur. Practice a sense of empowerment and the joy of success.

6. **Successful entrepreneurs never give up:** Giving up is not part of the vocabulary of the successful entrepreneur. "Even impossible means- I M Possible". Yet, smart entrepreneurs realize that time is not always favourable. One has to accept the ebb and flow of things—without giving up too soon. Successful entrepreneurs have the qualities of faith, trust, confidence and determination. To stay focused, they seek out the support of those who know them, encourage them and bring out their natural zeal. Successful entrepreneurs do not resist the change.

## 16.6. LEADERSHIP TRAITS OF SUCCESSFUL ENTREPRENEURS

In the past, managers were expected to maintain the status quo in order to move ahead. However, the ever-changing business environment asks for new forms of leadership. New leaders have to be visionary. They are both learners and teachers. They have to effect paradigm changes in society, be ethically strong and build integrity in their organizations.

Raymond Cattell, a pioneer in the field of personality assessment, developed the Leadership Potential equation in 1954. Today, this equation, based on a study of military leaders, is used to determine the traits that define an effective leader. These traits, which also apply to entrepreneurs, include the following:

1. **Emotional stability:** Good leaders must be able to tolerate frustration and stress. Overall, they must be well adjusted and have the psychological maturity to deal with anything they are required to face. They must have emotional intelligence.
2. **Dominance:** Leaders are often times competitive and decisive, and usually enjoy overcoming hurdles. Overall, they are assertive in their thinking style as well as their attitude in dealing with others.
3. **Enthusiasm:** Leaders are usually seen as active, expressive and energetic. They are often very optimistic and open to change. Overall, they are generally quick and alert, and tend to be outgoing.
4. **Conscientiousness:** Leaders are often dominated by a sense of duty and tend to be very exacting in character. They usually have a very high standard of excellence and an inward desire to do their best. They also have a need for order and self-discipline.
5. **Social boldness:** Leaders tend to be spontaneous risk-takers. They are usually socially aggressive and generally thick-skinned. Overall, they are responsive to others and tend to be high in emotional stamina.
6. **Tough-mindedness:** Good leaders are practical, logical and to-the-point. They tend to be low in sentimental attachments and comfortable with criticism. They are usually insensitive to hardship.
7. **Self-assurance:** Self-confidence and flexibility are common traits among leaders. They tend to be free of guilt and have little or no need for approval. They are generally secure and are usually unaffected by prior mistakes or failures.
8. **Compulsiveness:** Leaders are found to be controlled and very precise in their social interactions. Overall, they are very protective of their integrity and

reputation, and consequently tend to be socially aware, abundant in foresight, and very careful in making decisions or determining specific actions.

Beyond these basic traits, leaders of today must also possess traits that will help them to motivate others and lead them in new directions. Leaders of the future must be able to envision the future and convince others that their vision is worth following. To do this, they must have the following personality traits:

(i) **High energy**: Long hours and some travel are usually a pre-requisite for leadership positions, especially when a company grows. They remain alert and staying focused.

(ii) **Intuitiveness**: Rapid changes in the world combined with information overload result in an inability to 'know' everything. Leaders are increasingly learning to use their intuition and to trust their skills while making decisions.

(iii) **Maturity**: To be a good leader, personal power and recognition must be secondary to the development of employees. In other words, maturity is based on recognizing that more can be accomplished by empowering others instead of ruling others.

(iv) **Team orientation**: New business leaders put a strong emphasis on team work. Instead of promoting an adult/child relationship with their employees, leaders create an adult/adult relationship which fosters team cohesiveness.

(v) **Charisma**: People usually perceive leaders as larger than life. Charisma plays a large part in this perception. Leaders who have charisma are able to arouse strong emotions in their employees by defining a vision that unites and captivates them. Using this vision, leaders motivate employees to reach toward a future goal by tying the goal to substantial personal rewards and values.

### 16.6.1 A few renowned names of woman entrepreneurs

1. **EKTA KAPOOR (Birth: June 7, 1975)**: She was not interested in academics and on the advice and financial support of her father ventured into TV-serial production by the name of Balaji Creations at the age of 19 and soon she changed the face of Indian television industry and completely dominated it.

   *Achievement:*

   - Creative Director of Balaji Telefilms.
   - Awarded with Ernst & Young (E &Y) Startup Entrepreneur of the Year award in 2001.

2. **RITU KUMAR (Birth: November 11, 1944 Place of Birth: Amritsar)**: She was the first woman to bring the boutique culture to India, under the name "Ritu". The ace designer had a humble beginning in a small village, near Kolkata, in 1960, with hand block printers and two tablets to flaunt about.

   *Achievement:*

   - The most outstanding evening gown in international pageants.
   - Lifetime Achievement Award by the National Institute of Fashion Technology in 1998.
   - The Outstanding Women Entrepreneur Award by the PHD-Chamber of Commerce in 1998.
   - The Lifetime Achievement Award by the Kingfisher group.

3. **SHAHNAZ HUSSAIN.** CEO of Shahnaz Herbals Inc. A prominent Indian female entrepreneur best known for her herbal cosmetics, particularly skincare products.

*Achievement:*

- In the year 1977 she established her first beauty salon in her abode.
- Currently, the Shahnaz Husain Grouphas over 400 franchise clinics across the world covering over 138 countries.

*Award:*

- Success Magazine's World's Greatest Woman Entrepreneur.

4. **INDRA NOOYI:** Indra Nooyi born on October 28, 1955 in Chennai, Tamil Nadu having Indian Citizenship studied in United States Alma mater Madras Christian College and IIM Kolkata . She is a Chairman & CEO of PepsiCo.

*Award:*

Padma Bhushan 2007.

5. **Dr. KIRAN MAZUMDAR SHAW:** Birth: March 23, 1953 in Bangalore. Chairman & Managing Director of Biocon Ltd.She founded Biocon India with a capital of Rs. 10,000 in 1978. In 2004, she became India's richest woman.

*Awards:*

- Ernst & Young Entrepreneur of the Year Award in Healthcare & Life Sciences Category (2002).
- The Economic Times Business Woman of the Year Award (2004).
- Lifetime Achievement Award from Indian Chamber of Commerce (2005).

## REVIEW QUESTIONS

1. What is professionalism? Explain the elements of professionalism.
2. What do you mean by family entrepreneur? Explain the feature of family entrepreneur.
3. What is the difference Professionalism vs family entrepreneurs.
4. What do you mean by Woman entrepreneur? Explain the functions of women entrepreneurs.
5. Explain the role of women as an entrepreneur's.
6. Explain a few renowned woman entrepreneur names in India.

# Previous Year Paper Most Frequently Asked Questions

**AU/IP/ME/TX/CM-501**

## UNIT I : SYSTEM CONCEPTS

1. Define system. Draw a figure and explain the characteristics of systems.
2. Differentiate between natural and man-made systems. Give four examples.
3. Explain super and sub systems. What is key component?
4. What is interface?
5. Explain feedback /pull control in a system.
6. Explain feed forward /push control in a system.
7. Explain whether computer is an open or closed system.
8. What is law of requisite variety and its implications?
9. Draw Steven Alter's nine element work system model.
10. Discuss input-processing-output model open organization viewed as a system.
11. Write short note on-Four step system analysis process.

## UNIT II : MANAGEMENT

1. List and describe management functions.
2. What is management? List theories of management and explain any one.
3. Explain three levels of planning and their usual durations.
4. Explain BCG matrix and its implication.
5. List steps in decision-making.
6. Explain relation between authorities and responsibilities.
7. Explain business process reengineering and when it is required.
8. Draw a leadership grid and explain.
9. What is motivation? Explain Maslow Herzberg theories.
10. Explain Mintzberg's organization typology with a figure.
11. Define and explain corporate culture and its type.
12. Describe the concept of organization structure .What are the needs for organization structure?

## UNIT III : MARKETING

1. Differentiate between need, want and demand.
2. What a demand-supply forces and their effect on cost?
3. What is the importance of relationship in marketing?
4. Explain four P's of marketing-product, price, promotion and placement.
5. What are CRM and its importance?
6. List forms of business ownership and explain any one.
7. What is a balance sheet? Explain its components.

8. How profit and loss accounts are prepared?
9. Explain break-even point with a sketch.
10. What are payback period and NPV?
11. Define marketing and give its importance .
12. Explain holistic marketing concept and its components in brief.
13. What is an advertising medium ? Enlist various advertising media.
14. Give procedure and objectives of marketing research.
15. Give meaning and importance of capital budgeting .

## UNIT IV : PRODUCTIVITY AND OPERATIONS

1. Define productivity.
2. What are correlation between productivity, standard of living and happiness?
3. Explain basic production processes on product variety vs. volume diagram.
4. Explain suitable basic layout for basic production processes.
5. What is method study and why it should be done before time measurement?
6. What is rating and its importance in time measurement?
7. What is importance of time standards and what are various allowances in it?
8. Draw a graph to show relation between cost and quality of the product.
9. What is Taguchi's loss function?
10. Explain Six-Sigma quality and process capability?
11. Explain the relationship between production and productivity.
12. Enlist the factors influencing productivity. Explain how each factor will affect productivity.
13. What are the benefits from increasing productivity?
14. What is operation and project management?
15. What are various rating scales used in time study?
16. Explain about BMTS.

## UNIT V : ENTREPRENEURSHIP

1. Define and explain entrepreneurship.
2. Compare attributes of an entrepreneur with a manager.
3. Describe classification of an entrepreneur.
4. What is function of entrepreneur?
5. List economic theories of entrepreneur and explain any one.
6. List cultural theories of entrepreneur and explain any one.
7. Explain project idea / opportunity analysis by SWOT.
8. List any eight basis of product selection by entrepreneurs.
9. Describe sources of finance for entrepreneurs.
10. Why government is stressing EDP?
11. Name and explain important entrepreneurial traits.
12. What are various types of funds?
13. Briefly discuss the role of entrepreneur in bringing about social stability.

# MODEL QUESTION PAPERS

## Model Question Paper No. I

### ENTREPRENEURSHIP AND MANAGEMENT CONCEPTS

**501 (N) B.E.**

*Attempt one questions form each unit.*
*All questions carry equal marks.*

**UNIT I**

Q.1. (*a*) Define system. Draw a figure and write important characteristics of systems.

(*b*) Differentiate between natural and man-made systems. Give four examples.

**Or**

Q.2. (*a*) Discuss input-processing-output model open organization viewed as a system.

(*b*) Draw Steven Alter's nine element work system model.

**UNIT II**

Q.3. (*a*) What is management? List theories of management and explain any one.

(*b*) Explain BCG matrix and its implication.

**Or**

Q.4. (*a*) Draw a leadership grid and explain.

(*b*) What is motivation? Explain Maslow Herzberg theories.

**UNIT III**

Q.5. (*a*) Differentiate between need, want and demand.

(*b*) Explain four P's of marketing-product, price, placement and promotion.

**Or**

Q.6 (*a*) What is a balance sheet? Explain its components. How profit and loss accounts are prepared?

(*b*) What are CRM and its importance?

**UNIT IV**

Q.7. (*a*) Define productivity. What is method study and why it should be done before time measurement?

(*b*) What are correlation between productivity, standard of living and happiness?

**Q.8.** **(*a*)** **Explain Six-Sigma quality and process capability?**
**(*b*)** **Explain the relationship between production and productivity.**

**UNIT V**

**Q.9.** **(*a*)** Define and explain entrepreneurship. What is function of entrepreneur?
**(*b*)** List economic theories of entrepreneur and explain any one. List cultural theories of entrepreneur and explain any one.

**Or**

**Q.10.** **(*a*)** Explain project idea / opportunity analysis by SWOT.
**(*b*)** List any eight basis of product selection by entrepreneurs. Describe sources of finance for entrepreneurs.

*Attempt one questions form each unit.*
*All questions carry equal marks.*

## UNIT I

**Q.1.** (*a*) What is law of requisite variety and its implication?

(*b*) Differentiate between natural and man-made systems. Give four examples.

**Or**

**Q.2.** (*a*) What is interface? How many interfaces will be there among five subsystems?

(*b*) Explain feedback/ pull control in a system. Explain whether computer is an open or closed system.

## UNIT II

**Q.3.** (*a*) Draw a leadership grid and explain.

(*b*) Explain the importance and methodology of SWOT analysis. Enumerate the types of various decisions.

**Or**

**Q.4.** (*a*) What do you understand by" motivation ? Explain Mas low's hierarchy of needs,

(*b*) Explain in brief different types and level of planning.

## UNIT III

**Q.5.** (*a*) What do you understand by break-even point and pay back period?

(*b*) What do you understand by customer relationship marketing (CRM) ? What strategies help in identifying the customer base.

**Or**

**Q.6.** (*a*) What is the importance of relationship in marketing?

(*b*) Differentiate between need, want and demand?

## UNIT IV

**Q.7.** (*a*) Explain suitable basic layouts for basic production processes.

(*b*) Differentiate between project management and operation management.

Q.8. (*a*) Define productivity and range of its values.

(*b*) What are correlations between productivity, standard of living a happiness?

## UNIT V

Q.9. (*a*) What are functions of an entrepreneur?

(*b*) List any eight basis of product selection by entrepreneurs

Or

Q.10. (*a*) Describe sources of finance for entrepreneurs,

(*b*) Why government is stressing EDP?

# EXAMINATION PAPERS

## EXAMINATION, Dec. 2009

### ENTREPRENEURSHIP AND MANAGEMENT CONCEPTS

**Note :** (1) *Answer concisely to the point and use many figures.*
(2) *Answer any five parts out of ten parts in each of 1 to 5 questions.*
(3) *All question carry equal marks 4 to be answered in about a page*

### UNIT I

Q.1. (*a*) Define system. Draw a figure and write important characteristics of systems.

(*b*) Differentiate between natural and man-made systems. Give four examples.

(*c*) Explain super and subsystems. What is key component?

(*d*) What is interface? How many interfaces will be there among five subsystems?

(*e*) Explain feedback/ pull control in a system.

(*f*) Explain feed forward/push control in a system.

(*g*) Explain whether computer is an open or closed system.

(*h*) What is law of requisite variety and its implication?

(*i*) Draw Steven Alter's nine element work system model.

(*j*) How structure and performance of system and products lead to customer delight?

### UNIT II

Q.2. (*a*) What is management ? List theories of management and explain any one.

(*b*) Explain three levels of planning and their usual durations.

(*c*) List and describe management functions.

(*d*) Explain relation between authority and responsibility.

(*e*) Explain BCG matrix and its implication.

(*f*) List steps in decision-making. What are structured and unstructured decisions?

(*g*) Explain Mintzberg organization typology with a figure.

(*h*) Explain Business Process Reengineering and when it is required.

(*i*) What is motivation? Explain Maslow and Herzberg theories,

(*j*) Draw a leadership grid and explain.

## UNIT III

Q.3. (*a*) Differentiate between need, want and demand?
(*b*) What are demand supply, forces and their effect on cost?
(*c*) What is the importance of relationship in marketing?
(*d*) Explain four P's of marketing- product, price, promotion and placement.
(*e*) What is CRM and its importance?
(*f*) List form of business ownership and explain any one.
(*g*) What are contents of a balance-sheet?
(*h*) How profit and loss accounts are prepared?
(*i*) Explain Break-even-Point with a sketch,
(*j*) What are payback period and NPV?

## UNIT IV

Q.4. (*a*) Define productivity and range of its values.
(*b*) What are correlations between productivity, standard of living and happiness?
(*c*) Differentiate between project management and operation management.
(*d*) Explain basic production processes on product-variety vs volume diagram.
(*e*) Explain suitable basic layouts for basic production processes.
(*f*) What is method study and why it should be before time measurement?
(*g*) What is rating and its importance in time measurement?
(*h*) What is importance of time standard and what are various allowances in it?
(*i*) Draw a graph to show relation between cost and quality of a product,
(*j*) Explain Six-Sigma quality and process capability.

## UNIT V

Q.5. (*a*) Define and explain entrepreneurship ?
(*b*) What are functions of an entrepreneur?
(*c*) Compare attributes of an entrepreneur with a manager.
(*d*) Describe classification of an entrepreneur.
(*e*) List of economic theories of entrepreneur and explain any one.
(*f*) List cultural theories of entrepreneur and explain any one.
(*g*) Explain project idea / opportunity analysis by SWOT.
(*h*) List any eight basis of product selection by entrepreneurs.
(*i*) Describe sources of finance for entrepreneurs,
(*j*) Why government is stressing EDP?

## UNIT I

Q.1. (a) Explain work system theory.

Or

Q.2. Write short notes on the following:

(a) 4 P's of marketing

(b) Break-even point

(c) Business process re-engineering

(d) Advertising and publicity.

## UNIT II

Q.3. "Management is the effective utilization of human and material resources to achieve enterprise objective." Comment.

Or

Q.4. Explain the importance and methodology of SWOT analysis. Enumerate the types of various decisions.

## UNIT III

Q.5. What is Customer relationship management? How does it help in expansion of business?

Or

Q.6. The initial investment on fire fighting equipment is 56 ,125.The cash flows of five year are:

| Year | Cash flow |
|---|---|
| First | 14,000 |
| Second | 16,000 |
| Third | 18,000 |
| Fourth | 20,000 |
| Fifth | 25,000 |

At 10 % discount rate. Calculate payback period, net present value and also decide whether this investment is feasible or not .

## UNIT IV

Q.7. What do you understand by just in time production? Explain the advantages and disadvantages.

Or

Q.8. What is Six-Sigma? Enumerate the benefits of using Six-Sigma.

## UNIT V

Q.9. Differentiate between entrepreneur and manager with suitable example .

Or

Q.10. What are the various sources of fund and also discuss the entrepreneur development programme ?

# EXAMINATION, June 2011

## ENTREPRENEURSHIP AND MANAGEMENT CONCEPTS

*Time: Three Hours* *Maximum Marks : 100*
*Answer any one question from each unit.* *Minimum Pass Marks : 35*
*All questions carry equal marks.*

**UNIT I**

Q.1. (*a*) Explain in brief the law of requisite variety.
(*b*) What are the key components of a system? Explain in brief.

Or

Q.2. Explain Steven-Alter's nine element work system model.

**UNIT II**

Q.3. (*a*) Explain BCG matrix ?
(*b*) What are the steps involved in decision-making ? Explain in brief.

Or

Q.4. (*a*) What do you understand by motivation ? Explain maslow's hierarchy of needs.
(*b*) Explain in brief different types and level of planning .

**UNIT III**

Q.5. (*a*) What do you understand by customer relationship marketing (CRM) ? What strategies help in identifying the customer base.
(*b*) Explain the concept of fund flow. Why it is important for an industry ?

Or

Q.6. (*a*) Explain in brief the four P's components of marketing mix .
(*b*) What do you understand by break-even point and pay back period ?

**UNIT IV**

Q.7. (*a*) Explain in brief the steps followed in method study and method improvement.
(*b*) What do you understand by Six-Sigma quality ?

Or

Q.8. (*a*) Define time measurement and various various allowance provided in estimation of standard time .
(*b*) Explain in brief the concept of TPM.

**UNIT V**

Q.9. (*a*) What are the theories of entrepreneurship. Explain any one in brief.
(*b*) What rare the characteristics of successful entrepreneurs ?

Or

Q.10. (*a*) What are the role of an entrepreneur in generating employment Opportunities ?
(*b*) What are the objectives of entrepreneurial development programmes? Explain in brief the steps and relevance of ED's.

# EXAMINATION, Dec. 2012

## ENTREPRENEURSHIP AND MANAGEMENT CONCEPTS

*Time: Three Hours* — *Maximum Marks : 100*
*Minimum Pass Marks : 35*

*Note : Attempt One question from each unit.*
*All questions carry equal marks.*

### UNIT I

Q.1. Define feedback (pull) & feed forward (push) controls? Explain about open and closed system? 20

**Or**

Q.2. Write short notes on 20
(*a*) Profit and loss account
(*b*) Six Sigma

### UNIT II

Q.3. "Organization chart provides a broad picture of authority and their relationships in organizations structure". Discuss and describe the limitation of organization chart? 20

**Or**

Q.4. Explain Maslow's theory of need hierarchy? 20

### UNIT III

Q.5. Define marketing management? How finance management play an important role in marketing management? 20

**Or**

Q.6. The initial investment on a fire fighting vehicle ₹ 56125. The cash flow for five years are: 20

| Year | First | Second | Third | Fourth | Fifth |
|---|---|---|---|---|---|
| Cashflow | 14,000 | 16,000 | 18,000 | 20,000 | 25,000 |

at 10% discount rate. Calculate pay back period and net present value? Also decide weather this investment feasible or not?

### UNIT IV

Q.7. How does the production and operation management functions distinguish itself from other function of management? 20

**Or**

Q.8. What is total quality management (TQM)? How TQM play an important role in an organization? 20

### UNIT V

Q.9. Explain the theory of an entrepreneur? 20

**Or**

What are the available sources of funds for an organization, explain. 20

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